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Editorial Comment

The Dominion-Provincial Conferences

In the course of Dominion-provincial negotiations affecting the fate of the taxpayer in Canada, the Dominion pledge of provincial subsidies, which of course can be met only by extraction from the taxpayer, has according to press reports been moved up to successive new highs, while the morale of the taxpayer himself, as he sees his future thus mortgaged, has declined to successive new lows. There was a time when dictators or sovereigns used to farm out the tax raising power to favorites or supporters which tended to bid it up to all the traffic would bear. Now the Dominion government, in its anxiety to centralize the income tax at least, and apparently many other taxes as well, is being crowded by the provinces for the maximum "upset" price for such concessions. Regardless of whether the Dominion or the provinces should determine the rate and collect a tax, the tendency or effect of subsidies, fixed on a per capita or on some other rigid basis, is to increase the non-controllable part of the public budget. A province gets money to spend whether it needs it or not, while the Dominion in turn must exploit the tax source all the more in order to get money to spend on its own account. We can almost visualize the taxpayer on the auction block,

where his paying ability is being revised upward, while the governments pledge themselves to the expenditure of more and more money for his benefit, and his own spendable margin is successively reduced. The farther we go in this direction, the more we preclude hopes of general government economy.

*Is Public
Economy
Possible?*

With each increase in the subsidy offers to provinces, the uncontrollable part of our public budgets increases by many millions of dollars. Back in 1944 it looked as if the Dominion government might have a post-war budget of \$1,400 million while the provinces and municipalities might continue at their pre-war level of about \$600 million, which would make total public spending of two billion, and that is about all the traffic would bear. Since then, the Dominion government of its own accord has greatly expanded its social security program, and now proposes a spending level of close to two billion on its own account. And instead of one form of spending precluding another, they appear instead to grow by what they feed on, and the provinces are inclined to increase rather than reduce their own plans. The net result is that in little more than a year we find our governments figuring on a level of perhaps three billion instead of two billion of public money to spend. This is difficult to reconcile with a program of tax reduction, incentive to private enterprise, and a stable level of prices and wages.

*Views From
Down Under*

From the countries away down under—Australia and New Zealand — which in some schools of thought have been highly praised for their socialistic measures, there arrived at our Association office two publications which are far from in accord with this trend. Of course there is no gainsaying the fact that socialism is strong in these two countries, even more so than in America, so we can not accept these publications as any more than sectional or class representations.

One is entitled "The Taxpayer" and though described as the official organ of The Taxpayers' Association of Victoria, it refers also to views expressed in other Australian

states, and to urgent demands throughout the commonwealth for modification of the tax burden.

The other publication is "New Zealand Commerce", the official organ of the Associated Chambers of Commerce of New Zealand, and even a slight knowledge of New Zealand entitles us to respect the plight of any chamber of commerce located there. From the pleas for relief from the excess profits, social security and other impositions, it is evident that private enterprise in New Zealand, which according to latest information had very little margin over state enterprise, is now putting up a battle for survival.

*The Senate
Tax Inquiry*

In this issue we publish part of the Senate tax committee evidence regarding discretionary power. Though running to considerable space in our magazine, this is still a mere fraction of the 327 pages of proceedings of the committee. That was for seven sessions, held in November and December. Being a committee of one of our houses of parliament, it could not function when parliament was not in session, and therefore will resume when parliament meets again in March. Four of the seven committee sessions were occupied with detailed exposition by C. Fraser Elliott of the Dominion tax administration and with exhibits filed as part of this evidence. At the other three sessions there were submissions by organizations and individuals interested in the work; while these did include some administrative points, they tended to drift into economic arguments which are outside the scope of the committee. Numerous other bodies are to appear before the committee when it resumes, and The Dominion Association of Chartered Accountants plans to be among them. The inquiry is helping to clear the air of many erroneous ideas concerning the tax machinery, and it is hoped that it will result in some practical conclusions.

Bankers' Comments on Taxation

A Symposium of Views Expressed at Recent Annual Meetings of Canadian Banks

COMMENTS of Canadian bankers at their recent annual meetings, on taxation and related financial matters, are reproduced below, because of the outstanding public concern regarding these problems at the present time.

Bank of Montreal, December 3, 1945

(From address of President G. W. Spinney)

In time of war it has been possible to divert to the state a fantastically large proportion of the product of the effort of the individual citizen. The public in wartime have been ready and willing to make the sacrifice in living standards which high taxation involves, because of overwhelming acceptance of the necessity of a supreme effort for survival.

The peacetime background will be different. The various items of expenditure will not by any means command the same degree of unanimous approval, and once consumer goods are again available in adequate quantities it will be difficult for the individual to comprehend why, through the impact of heavy taxation, his own buying power should be reduced. Under such conditions the limits within which the product of individual effort may be redistributed by legislative action, no matter for what praiseworthy purpose, become very much narrower than in wartime.

If we ignore this fact, the result cannot fail to be diminished incentives, dislocation and discontent, and a strong upward pressure on costs of production—matters of considerable moment in relation to our post-war objectives of a high level of production and employment at home, and an expanding external trade.

Bank of Nova Scotia, December 5, 1945

(From address of President H. D. Burns)

The problems inherent in the sudden changeover to peace and the difficulties of timing the removal of wartime measures are also reflected in the first post-war budget. Here a balance had to be struck between the continuing risk of inflation and the risk of restricting reconversion and economic expansion. Thus, on the one hand,

taxes directly restricting incentive and initiative were considerably reduced and a moderate cut was made in the extremely high rates on personal income. On the other hand, tax concessions were limited, because of the continuing danger of inflation and of the prospective high rate of government outlays.

The Minister of Finance emphasized the clear restrictive effect of the excess profits tax on business expansion and "as an interim step toward the ultimate abolition of the excess profits tax" proposed a reduction in the rate to 60% and made provision for raising the standard profits of small businesses. These changes are constructive and should do much to stimulate employment-creating activities, more especially since they are combined with the assurance that the excess profits tax will ultimately be removed.

It should be noted, however, that the question of Dominion-Provincial relations and responsibilities still beclouds the taxation outlook and indeed affects Canadian economic prospects in a number of important ways. A Dominion-Provincial settlement is, in my opinion, one of our most urgent post-war tasks. It is perfectly true that difficult political questions are involved. But it is also true that failure to arrive at a settlement, conceived with imagination and appropriate to the social and economic conditions of the times in which we live, would restrict our economic progress and indefinitely delay the realization of a balanced program of social security. Whether or not we agree with the proposals made by the Dominion government for a settlement, these do represent a sincere and vigorous effort to deal realistically with problems that can now be evaded only at great cost and with much friction.

Let us remember that failure to reach a settlement could seriously impede our progress in the immediate transition and affect adversely our welfare in years to come. Continued uncertainty in regard to taxation is a present serious barrier to enterprise and to high employment. The difficulty of arriving at financing arrangements between governments for needed public works, which is inherent in the present state of doubt as to the division of responsibilities and jurisdiction, is also a matter for grave concern. It might mean that for lack of planning and pre-

paration necessary public works could not be commenced when and where they might be required to sustain economic activity.

(From address of General Manager H. L. Enman)

The president has already said something about certain of the broad aspects of taxation. I should like to add a few words about the necessity of improving the administration of the corporate income taxes, for in the day-to-day conduct of the bank's affairs we naturally see and learn a good deal about the tax problems of Canadian business. The complicated tax structure and the degree of latitude in administrative decision, combined with the wartime shortage of trained staff, has resulted in delays in the settlement of taxes and in decisions on particular tax questions, which have become a very serious matter. So long as the war continued, these delays, often running for a matter of years, were understandable. But a continuation of these unsatisfactory conditions in the postwar period would have the unfortunate consequence of restricting business expansion. There are quite enough unavoidable uncertainties in the business outlook today without adding one which can be corrected by improved tax regulations and administration, and it is to be hoped that early action will be taken to speed up tax settlements.

Bank of Toronto, January 16, 1946

(From address of President F. H. Marsh)

Inseparable from the question of government ownership and government control is that of taxation. Its heavy burden arises from war costs and other accumulated obligations, from losses incurred through public ownership, from the narrowing of the tax base through exemptions, and from the vast civil establishment operated for general government. Any progressive economy requires a high degree of productive efficiency and a substantial degree of saving, both of which are possible only under the stimulus of adequate incentives. Yet we place a considerable part of our activities outside the area in which these incentives can take full effect. The income and excess profits tax rates have created, in both individuals and corporations, a marked desire for safety in preference to the risk which would be involved in justifiable industrial expansion. Thus indeed new avenues of employment are

restricted. Under the stress of war, our tax methods were permeated by the principle of catch as catch can. To continue such imposts would mean expecting too much of too little, and one of our first domestic concerns is a radical reform of our tax system with a view to setting a reasonable level of taxation and choosing levies which will allow adequate scope for both enterprise and thrift.

Banque Canadienne Nationale, January 8, 1946

(From address of President Beaudry Leman)

The proposals submitted by the Federal authorities at the two interprovincial conferences which were held in Ottawa in the course of 1945, entailed the maintenance of measures whereby the central power would levy and collect income taxes on corporations and individuals. Briefly, the Minister of Finance, who already held the title of Receiver General of Canada, would also become the Paymaster General of the Country. These questions are under scrutiny and their importance is such that it is quite understandable that the provinces should study them with wariness, carefully surveying the avenues of their further progress.

These proposals, at least in principle, would be acceptable to the Canadian business world which shuns the multiplicity of collecting agencies. A system of imposts which would be uniform, coherent, simple and understandable, extending throughout Canada, would present unquestionable advantages. There are, however, other aspects of this question. Each province carries its own responsibilities and must face its own particular problems, each must find the necessary resources for purposes of education, hygiene, health, social progress, as well as for the development of its natural resources. The duties which rest upon each individual province cannot be delegated to the Federal authority any more than their accomplishment can rest solely upon the generosity or the discretion of the central government. The state has assumed burdens which must be discharged, but the provinces also have pressing obligations; inasmuch as the taxable resources of this country are not unlimited, an understanding between governments is imperative. Moreover, burdensome taxation, whether it originates from the federal or from provincial governments, may well paralyse economic activity, hinder

commerce and would dry up in short order the revenues upon which public bodies depend to meet their obligations. The Federal government should not appropriate too large a share of the product of taxation as such a policy would almost inevitably drive the provinces to the taking over of profitable enterprises. All interested parties would be worse off if the proposals now submitted were to result in the development of socialization or—to employ another term which some prefer—in the nationalization not only of public utilities, but of other kinds of undertakings. Several provinces are already engaged, apart from public services, in the insurance business, in railway operations, in the liquor trade and what not. Events and politics have an inescapable logic.

Canadian Bank of Commerce, December 11, 1945

(From address of President Allan E. Arscott)

During the early part of the war it was suggested by fiscal authorities that taxation be utilized among other things for the purpose of directly siphoning off excess purchasing power. Whether for revenue purposes or to reduce the expendable currency in the hands of the public, the impact of taxation on the individual is to restrain purchasing; on the corporation it may tend to retard productive output. Obviously there are limits beyond which taxation cannot be pushed; incentives must not be neglected in fiscal planning.

Over the past few years we have moved into an era of "fiscal control".

During the first part of the present century the ideal of a small and balanced budget became modified. Increasingly heavy tax structures became common, partly because of the exigencies of war and partly as a result of a widespread acceptance of expenditures on objects deemed to be of social benefit. The view that the public budget should be neutral in its effect upon the economic structure depended essentially on the premise that the total revenues and expenditures collected and disbursed by government should be small, say not more than five to ten per cent of the national income. This was roughly the case in Canada up to the beginning of the second world war. In 1939, for example, with an estimated national income of about \$4.5 billion, the Dominion budget was in the neighbourhood

of half a billion dollars, or slightly over ten per cent of the national income. However, during the war years the estimated national income has about doubled and even if that level could be maintained a conservative estimate of Dominion government requirements would seem to be in the neighbourhood of twenty-five per cent of the national income.

Under such circumstances the budget cannot be neutral. The aggregate of government tax revenues has increased to the point where it has become a substantial factor in costs, and public disbursements at the same time have become a factor in the level of employment. At such levels taxes can hardly be devised which will not exert an influence upon both the amount and direction of private spending and investment.

Given these conditions, it has come to be quite widely held that the balancing of budgets on the traditional annual basis may no longer be possible without accentuating other tendencies which may lead to periodical instability of business. It is therefore being advocated in some quarters that in place of attempting to achieve a rigidly balanced budget on an annual basis, the appropriate policy for governments would be to aim for balance over some longer term than a fiscal year. This viewpoint contemplates that deficits would be incurred in depressed years while surpluses would be budgeted for in years of relative prosperity.

It will be realized that in adopting a policy of cyclical budget balancing, involving shifts in tax emphasis and deficit spending, a government is venturing into largely uncharted waters and the question arises as to what indicators are to be used to determine whether in any given year, the government should budget for a surplus or for a deficit. Incidentally, it is not hard to see how difficult it might prove politically to implement heavier taxation and/or the curtailment of public expenditure, even should all indicators suggest the desirability of such a policy. The whole subject is one which demands much thought and study not only by governments but by all business groups, including both labour and management, who are affected by the impact of taxation.

Dominion Bank, December 12, 1945

(From address of President C. H. Carlisle)

The liquidation of Canada's debt, the carrying charges on the indebtedness and the cost of government in its entirety is the direct responsibility and obligation of each citizen or resident of Canada. Each taxpayer and consumer should be recognizant of the fact that he and he only pays the bill. You may study the budget presented yearly to parliament and find that government receives revenue from tariffs, from excise taxes, from income taxes, succession duties, etc. The revenue received from tariffs and excise taxes is necessarily added, in part at least, to the cost of the goods, and selling prices are then established on the increased costs. The consumer pays! The revenue received from income taxes and succession duties is paid, either directly or indirectly, by the individual. You may hold stock in a company. The earnings of that company are taxed. You as a shareholder are also taxed on your dividends. In both cases you pay! The government has no funds of its own and only acts as your agent in incurring and paying your debts. You have given to government an unlimited power of attorney as to assessment and expenditure. Therefore, you undoubtedly have a direct and vital interest in government expenditures and in the obligations government creates for you.

How can our present debt and subsequent debts be paid?

To reduce a debt expenditures must be less than income.

There are two sources of income; one is production, the other is service.

Production is vital to the individual and to the nation. It is the major source of employment. It is the major source of revenue. It is especially vital to Canada, due to Canada's great resources, both developed and latent. Canada's production during the war was necessarily different to that of normal times. During war many products are produced that are not required in peacetime. War products are for immediate and temporary consumption. A great many products produced for peacetime consumption have a much longer duration. The cost of war production is necessarily excessive. There is a great deal of unavoidable waste. This excessive cost is reflected in our present

indebtedness, and forms a very material part of that indebtedness. Wartime costs must be reversed in peacetime production, or you increase your indebtedness. In doing this, you create inflation. Inflation is destructive in all of its aspects, as was plainly exemplified following the last war, when in some countries money became absolutely worthless.

It is necessary to reduce costs to reduce selling prices. More goods are produced and more goods are consumed on a lower selling price than on a higher selling price.

Imperial Bank of Canada, November 28, 1945

(From address of President R. S. Waldie)

It is true, the Dominion government has since 1942 collected by taxes about 30 per cent of the national income. But during the emergency of a war a high tax burden is more readily borne and shortcomings of the tax legislation are more leniently looked upon than in times of peace. For this reason the time has come for a thorough reform of the whole tax system. Those impositions which enter directly the cost of production, should be reduced and finally abandoned.

Tax reform appears all the more necessary since the number of countries, especially in Europe, which have inflated their currencies, has greatly increased as a result of the war, and is likely to increase further during the coming years. This development has automatically reduced Canada's competitiveness in the world markets.

There is a further reason for the removal of most indirect taxes except those directly borne by the consumer. If the former trend towards agricultural self-sufficiency is resumed in Europe after the recovery period, Canadian farm exports are likely to decrease once more as they did between wars. Exports of newsprint and other wood products are also endangered in the long run unless more efficient policies of reforestation and conservation are established. This means that metals and goods in more highly finished form are likely to comprise a greater proportion of Canada's export trade. But the many new indirect taxes introduced by war finance are most burdensome for manufacturing and mining and discourage venture capital and should be removed as should also those war con-

trols which tend to retard the return to normal economic activities.

The complex questions which the transition from war to peace impose on Canada can only be solved by the willing co-operation of all. The troubled conditions of the whole world are a clear indication of the magnitude of the tasks ahead. I sincerely trust Canada will not be lacking in that mutual confidence and willingness for work and sacrifice without which no country can hope to survive.

Provincial Bank of Canada, January 10, 1946

(From address of President Chas. A. Roy)

After so much spending during the past few years, it is to be hoped that the government will now so direct its economy as to give first place to the real interest of the country, and also that it will adopt fiscal and financial policies, that are constructive but sound. A reduction of expenses and the elimination of waste, a balancing of the budget and a reduced and better incidence of taxation are ways and means that will help to bring back those economic conditions which go to reduce the cost of living. A reduction of taxes on the salaries and wages of workers and a lowering of the cost of living would facilitate an adjustment of the problem of wages and selling prices. At the present time, these are a few among many conditions indispensable to the return of full industrial and commercial activity; their adoption would help make possible the marketing of products at competitive prices.

**Treatment of Inventory Values in
Financial Statements**

By C. S. Westthorp, C.A.

Newark, N.J.

GREATER emphasis has been placed in recent years on the valuation of inventories of merchandise, raw, partly processed or finished, than almost any other item appearing in the balance sheet. This is well justified by current conditions, wherein the inventories carried by numerous companies have not only increased greatly in both volume and value but have also undergone radical changes

in nature. For example, where the inventories of an aircraft company prior to the war might have included a few completed commercial aircraft together with a necessary small supply of parts, raw materials and partly processed stock, the inventories of the same company during the war years would have comprised not only a substantial quantity of military-type aircraft and related parts but also a large stock-pile of raw materials built up to meet current requirements and in anticipation of future orders and the possibility of short supply. The accountant, whether public or private, has been faced with the problem of reconciling two conflicting views—conservative accounting practice and a realistic presentation of costs.

The method of valuation generally adopted prior to 1940 was "the lower of cost or market". In order to meet the objective outlined above, this method has been substantially modified in many cases, and has been replaced by either the much-popularized LIFO method or that of the "basic inventory".

Cost or Market

Even the old tried-and-true method of valuing inventories on the basis of the lower of cost or market has been subjected to the keen light of criticism. This method has been attacked in all its parts: What is "cost", what is "market", and what is the justification for using either?

In the first place, cost has been interpreted as: 1. Actual cost to the company of individual articles ("first-in, first-out" or FIFO). 2. Average cost over a given period of time. 3. A moving average cost, based on the quantity remaining on hand. 4. Cost of the earliest purchase, with issues from stock being valued at the latest price (LIFO).

Secondly, market value has also been subject to varying interpretations, such as: 1. Cost of replacement on the open market. 2. Cost of replacement by the company itself, where a manufactured rather than a prime article is concerned. 3. Current selling price, less cost of completing and selling the product and, in some instances, less estimated profit.

All these methods have as their aim the idea of presenting in the balance sheet values for inventories at levels which may be realized on future sale, and of reflecting in

the profit and loss account the estimated cost of material consumed by production and sale.

Variations

The variations which have been introduced in recent years are designed to eliminate from inventories excessively costly materials in periods of rising prices, retaining basic stocks at lower or "pre-inflation" levels. In this respect the "LIFO" and "basic inventory" methods are identical; the variations between the two being in the retention by the latter of a minimum quantity at specified prices. The main purpose in using these methods is to provide a hedge against possible sudden or unexpected declines in prices, by charging materials at the highest cost against the greatest volume of production and leaving relatively cheaper materials to be used when volume and sales prices may be lower.

These methods of valuation are not in conflict with the basic accounting principle of conservative valuation, viz., to absorb all realized and expected losses and to anticipate no profits.

The other methods of determining cost are dictated very largely by the nature of the operations and the number and variety of articles which may be carried in stock at any given time. It may be impracticable to determine actual cost of individual issues of material, in which case average costs are used. The variations in interpretation of "market" also are usually dictated by the requirements and nature of the particular business or industry.

Basic Reasoning in Inventory Valuation

It would appear that all problems of inventory valuation have been approached with the idea of determining the amount at which they should be recorded in the balance sheet. Little or no consideration has been given to the effect on the profit and loss account of varying methods of valuation.

In the first place, what is cost? It must be the price paid for an article in money or other valuable consideration. Any other interpretation of cost results in a composite valuation. This composite valuation will contain, primarily, actual cost of the article; but it will also comprise either an inflation in value—anticipated profit—a hedge against a possible future price reduction, or some element

of the cost of another like article. If I buy 100 lbs. of sugar at 4 cents per pound and sell 50 lbs. at 5 cents per pound, my "cost of sales" is \$2 and my profit is 50 cents. If I then buy an additional 100 lbs. at $4\frac{1}{2}$ cents per pound, and dump this new lot into the bin containing the 50 lbs. remaining from the original purchase I have an inventory of 150 lbs. of sugar, not identifiable as to lot but costing on the average $4\frac{1}{3}$ cents per pound. If I should anticipate a decline in the price of sugar to its original level of 4 cents per pound, I could provide a reserve against that anticipated decline of 50 cents, leaving my inventory of 150 lbs. of sugar valued at 4 cents per pound. By reason of providing this reserve I have not in any way affected the cost of the sugar; that cost remains at $4\frac{1}{3}$ cents per pound. To reason that the market price of sugar may drop—or has already dropped—from $4\frac{1}{2}$ cents to 4 cents per pound and therefore that my inventory only cost me 4 cents per pound is fallacious. Such reasoning undoubtedly will result in a conservative balance sheet valuation for the inventory of sugar, but it has an unfortunate effect upon the profit and loss account.

The accountant sees no problem in the treatment of other items in the balance sheet which also bear a direct relationship to the profit and loss account. The fixed assets used in the business, for example, are continually in the process of consumption. Their cost is recorded in the books of the company at actual cost, valued in terms of money or money's worth. The "consumption" of fixed assets through their use in production is recorded as a charge against earnings by way of the provision for depreciation. If any special factors enter into their use, such as the possibility of obsolescence, a special provision is made for that contingency.

A similar analogy may be drawn in the case of accounts receivable. Provision is made in the profit and loss account for possible losses on collection of outstanding accounts, not by direct charge against sales, nor in the cost of sales, but as a separate item either in selling expenses or in the miscellaneous financial charges. The justification for this treatment is that such a charge bears no relation to the cost of production but is a responsibility of the financial section of the administration, and does not enter into costs or expenses until the sale is complete.

The same argument may be applied with equal force to the valuation of inventories. The purchase is complete and the cost of goods established when the complete product either has been purchased or has been manufactured in the plant. The fact that the financial officers of the company may decide that some reserve is necessary to provide for possible future inventory losses has no bearing on the cost of the article, and hence none on the cost of goods sold.

This position becomes even more apparent when inventories are valued "lower than cost or market". In this case, a definite reserve has been provided for future contingencies by a direct charge to cost of goods sold, through the device of deliberately undervaluing the inventories.

The consumption and creation of assets follow a direct line of flow. First, fixed plant is acquired; this is consumed in producing finished goods; the finished goods in turn become accounts receivable through sale; and the accounts receivable become cash. Yet in this whole sequence, accountants select one item—inventories—for special treatment in the profit and loss account. Any special depreciation in value which might be anticipated with regard to fixed assets or accounts receivable is provided for by a special charge, but a similar and directly comparable anticipated shrinkage in inventory values is charged against cost of sales without disclosure.

This situation has evolved from the use of double entry bookkeeping:

Debit inventories of merchandise

Credit cost of sales

To record *value* of inventory at 31/12/44.

It must be appreciated that the balance sheet and the profit and loss account are two distinct statements entirely different in nature. One is fixed in time and is intended as a "still-life picture" of the affairs of a company as of a given date; the other is a "motion picture" giving a review of the company's operations throughout a specified period. One is static, the other fluid; and the same values and interpretations cannot be made to prevail throughout the two.

This is not intended as a criticism of the more modern methods of inventory valuation. Each has its place and its use under varying circumstances. This is, however, a

INVENTORY VALUES IN FINANCIAL STATEMENTS

criticism of the practice of using those same values without further consideration in the profit and loss account. The difficulty may be resolved quite easily; all that is necessary is to show properly in the profit and loss account the provision for inventory shrinkage as distinct from the actual cost of goods sold. This provision will then take its rightful place among the financial charges and will not find itself buried in the valuation of inventories which are included in the cost of sales. By this method, any desired valuation of inventories may be used for balance sheet purposes to meet the needs of the industry, the particular company, and the times; but the cost of sales will be shown at cost and not at some more or less arbitrary value which represents cost plus or minus an adjustment in a reserve.

Under these circumstances the profit and loss account would appear as follows:

Sales		\$ x x x
Less cost of goods sold:		
Opening inventory at cost	\$ x x x	
Purchases	x x x	
	x x x	
Less closing inventory at cost	x x x	x x x
Gross profit		x x
Selling, general and administrative expenses		x x
		x x
Financial charges:		
Provision for bad debts	x x	
Provision for shrinkage in inventory valuation	x x	x x
Net Income	\$	x

The inventories would then appear in the balance sheet at the sum of their value at cost less the provision for shrinkage, with appropriate wording to describe such valuation, whether it be cost or market, LIFO, FIFO or any other method. If in a subsequent year the value of the inventories so determined were to rise in its relation to cost, and a net reduction in reserve were required, such valuation adjustment would appear under the heading of miscellaneous income and would be added to profits. In any event, inventories would appear in the balance sheet at the best available valuation and in the profit and loss account at cost. What else can cost of sales be *but* cost?

Discretionary Tax Powers

Extracts from evidence of C. Fraser Elliott, Deputy Minister of National Revenue for Taxation, before the Senate Tax Committee.

MR. ELLIOTT: A very important subject in the minds of the public is the delegation of authority to the deputy minister and the exercise of that authority under the provisions of the law, commonly referred to as exercise of discretion or discretionary powers.

The statutory authority is contained in section 75. This will be a dry subject, but I want to have it technically correct. Section 75, subsection 2 of the Income War Tax Act which is brought into the Excess Profits Tax Act by section 14 thereof reads as follows:

75(2) The minister may make any regulations deemed necessary for carrying this act into effect, including regulations designed to facilitate the assessment of tax in cases where the right of taxpayers to deductions or exemptions has varied during any taxation year, and may thereby authorize the Commissioner of Income Tax to exercise such of the powers conferred by this act upon the minister, as may, in the opinion of the minister, be conveniently exercised by the Commissioner of Income Tax.

On August 8, 1940, the then Minister of National Revenue, Colin Gibson, pursuant to the above subsection of section 75, caused to be published at page 852 of the Canada Gazette of September 13, 1941, the following:

IN THE MATTER OF THE INCOME WAR TAX ACT AND AMENDMENTS
AND

IN THE MATTER OF THE EXCESS PROFITS TAX ACT

To whom it may concern:

Be it hereby known that under and by virtue of the provisions of the Income War Tax Act, and particularly section 75 thereof, and the provisions of The Excess Profits Tax Act, 1940, and particularly section 14 thereof, that I do hereby authorize the Commissioner of Income Tax to exercise the powers conferred by the said acts upon me, as fully and effectively as I could do myself, as I am of the opinion that such powers may be the more conveniently exercised by the said Commissioner of Income Tax.

Dated at Ottawa this 8th day of August, A.D. 1940.

COLIN GIBSON (signed)

Minister of National Revenue.

By chapter 24 of the statutes of 1943-44, assented to July 24, 1943, and made applicable on passing, the Department of National Revenue Act was amended to provide for the appointment by the Governor in Council of a Deputy Minister of National Revenue for Taxation and a Deputy Minister of National Revenue for Customs and Excise. It was also provided that wherever in any statute, regulation, authorization or order, there appears the expression "Commissioner of Income Tax" or "Commissioner of Succession Duties" . . . the said statute, regulation, authorization or order shall be read and construed as if the expression "Deputy Minister of National Revenue for Taxation"

DISCRETIONARY TAX POWERS

were substituted for the expression "Commissioner of Income Tax" or "Commissioner of Succession Duties".

From the above it will be evident

(1) that the minister has the authority to delegate certain of his powers to the Commissioner of Income Tax;

(2) that the powers have been properly delegated to the Commissioner of Income Tax;

(3) that the Commissioner of Income Tax now means Deputy Minister of National Revenue for Taxation.

Quite apart from the fact of actual delegation, a deputy minister of the Department of National Revenue has virtually the same powers conferred upon him by statute as the minister has for administration purposes, of course, not for policy and parliamentary purposes.

Section 3, subsection (2) of chapter 24 of the statutes of 1943-44, assented to July 24, 1943, says:

3. (2) The Deputy Minister of National Revenue for Taxation shall be the lawful deputy of the minister, exercising power and authority as if he were deputy minister of a separate department of government charged with the control, regulation, management and supervision of internal taxes including income taxes and succession duties.

Thus the actual delegation by the minister is more useful as evidence of the scope of the authority than as a substantive document in its own right. In other words, we could get the authority in two ways, but the delegation by the minister is outward evidence of a factual condition.

The next question is whether the operation of the *maxim delegatus non potest delegare* requires the deputy minister, when exercising discretionary powers in the name of the minister, to do all the acts himself. The ancillary question is, of course, whether he may engage his subordinate officials in the course of their ordinary duties to prepare the matters for him without violating his delegation or exceeding his authority.

I would like to say a word on the jurisprudence of that question. In this connection the following excerpts from a few English and Canadian cases are helpful.

The first point is the use of subordinates. I quote from the case of *Local Government Board v. Arlidge*, (1915), A.C. 133, Viscount Haldane, L.C. stated:

The minister at the head of the board is directly responsible to parliament like other ministers. He is responsible not only for what he himself does but for all that is done in his department. The volume of work entrusted to him is very great and he cannot do the great bulk of it himself. He is expected to obtain his materials vicariously through his officials, and he has discharged his duty if he sees that they obtain these materials for him properly. To try to extend his

duty beyond this and to insist that he and other members of the board should do everything personally would be to impair his efficiency. Unlike a judge in a court he is not only at liberty but is compelled to rely on the assistance of his staff.

Now the second point is, production of these reports.

Lord Haldane also remarks, at p. 134, respecting the propriety of producing a report of a subordinate official relative to the exercise of discretion:

In accordance with that practice, the board, in order to obtain materials with which to decide, appointed one of its health inspectors to hold a public inquiry. This was in accordance with the rules it had made under the section of the statute which I have quoted and was its usual practice. It is said that the report of the inspector should have been disclosed. It might or might not have been useful to disclose this report, but I do not think that the board was bound to do so any more than it would have been bound to disclose the minutes made on the papers in the office before a decision was come to.

A further quotation of interest from the Arlidge case which was cited in the Exchequer Court of Canada in the decision of *Wrights Canadian Ropes Ltd. v. Minister of National Revenue* (1945), *Canadian Tax Cases*, p. 177 at p. 186, is as follows, where referring to a document Lord Shaw stated:

It may contain, and frequently does contain, the views of inspectors, secretaries, assistants, and consultants of various degrees of experience, many of whose opinions may differ but all of which form the material for the ultimate decision. To set up any rule that that decision must on demand, and as a matter of right, be accompanied by a disclosure of what went before, so that it may be weakened or strengthened or judged thereby, would be inconsistent, as I say, with efficiency, with practice, and with the true theory of complete parliamentary responsibility for departmental action. This is, in my opinion, implied as the legitimate and proper consequence of any department being vested by statute with authority to make determinations.

I should like to comment on the third point: The personal signature by the delegate is unnecessary: that is, the personal signature of the minister delegating his authority to me is not a *sine qua non*, it is not absolutely necessary.

In this connection see *West Riding County Council v. Wilson*, (1941), 2 All E.R., p. 831. I might say before reading this that in fact all matters pertaining to the delegation that I exercise in respect of the factual conditions reported to me by my staff, I sign them myself; no delegation is exercised without my signing it.

In the *West Riding* case Viscount Caldecote, Lord Chief Justice, remarked:

The letter of December 14th is signed by an official who was authorized, according to the letter, by the Minister of Agriculture and

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Fisheries, and I accept that as proof of the satisfaction of the condition that the minister's consent in writing must first be obtained.

The further point is taken that the letter from Hole is void because the minister had no power to delegate his responsibility to Hole. I do not read that letter in that way. Hole was authorized, according to the letter, by the Minister of Agriculture and Fisheries, and, in the absence of any evidence that he was not so authorized, I accept the letter as the letter of the minister, or as the consent of the minister in writing. It is not the case that all consents of ministers have to be signed by the ministers themselves. The business and the duties of ministers of the Crown would very often be quite impossible if they had to sign all the documents in which their consent was given or their opinion expressed.

I would also like to refer to the *Point of Ayre Collieries Ltd. v. Lloyd George*, (1943), 2 All E. R. p. 548.

HON. MR. DUPUIS: Is that an English case or a Canadian case?

MR. ELLIOTT: That is an English case. I should like to mention something about the rules which must be followed by any person who is exercising a power of discretion. The courts in Canada and England have formulated certain rules for the exercise of administrative discretion. These rules, which we have followed to the best of our ability, may be summarized as follows:

Discretion must be—

1. exercised on proper legal principles
2. exercised in a fair and honest manner.

Discretion must not—

1. be against sound and fundamental principles
2. take into account matters which are not proper for the guidance of the person exercising it.

So important have we considered the propositions which I have just mentioned to you that early in 1942 we prepared a set of internal instructions for our inspectors, explaining the principles to be followed in making any recommendations with respect to assessments which might depend upon the exercise of discretion. I refer you to page 2 of the internal office memorandum which I shall put in as exhibit no. 7 and have passed around in a moment.

I think if I may I would like to go to that memorandum now, because it is the working document in the field that the men are using, and I think we had better get close to the actual working of our division. This is a memorandum which, when you get it, will show you exactly how we carry out the exercise of discretionary powers. This is the usual practice in our division: there is no other way of sending

a memorandum to the nineteen inspectors across Canada, informing them how to behave in their work, and that is really what this is. While it is marked "strictly confidential" I would not like to withhold from this committee anything we have. The word "confidential" to this committee is really out. There is only one confidential thing in our division from this committee, and that is the individual and corporate returns of taxpayers. That word "strictly confidential" at the head of this statement is just out. May I read it, Mr. Chairman?

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The Income War Tax Act and the Excess Profits Tax Act provide in many cases for the exercise of some discretionary power by the minister. The cases arising frequently are those concerning the amount to be allowed for depreciation, salary, chief business under section 10, capital costs under section 90, etc., etc. Altogether there are about thirty discretionary sections or parts of sections.

Such discretionary powers must be exercised in a quasijudicial manner, that is to say, the person in whom the power is vested must

- (a) know the facts, or in cases under dispute, must
- (b) determine which are to him deemed to be the true facts;
- (c) have some reasonable knowledge of the law relating to the question at issue (as we all have because taxation is our business), and must
- (d) come to a fair and reasonable conclusion, after due consideration.

The courts have held that wherever a person is by an act of parliament given some power to be exercised at his discretion, he must observe the following rules.

(1) The discretion must actually be exercised in every individual case. It cannot be exercised by merely making a general ruling which would be applicable to all cases, although that may be used up to the point of confirmation in the particular case in active dispute.

In other words, you can give a general guide, but if it comes into question it must be exercised individually. The general guide is that we allow 10 per cent reserve, a 10 per cent depreciation on machinery. But it must come down to the individual exercise.

For instance, we have a rule that a certain maximum percentage for depreciation may be allowed on automobiles, but if any taxpayer should claim a larger amount for depreciation it would not be sufficient to cite the general rule but it would be necessary to look at all the facts in the particular case and then decide that the usual rates are reasonable in bringing out the amount to be allowed or if not, what is a reasonable amount in the circumstances.

- (2) The discretion must be exercised honestly and fairly.
- (3) The discretion must be reasonable and not arbitrary.
- (4) The power must not be used to recoup the Treasury for taxes which have been lost because of some transaction of the taxpayer not covered by the act. If part of a salary is disallowed it must be after a fair and honest review of the taxpayer's circumstances and because the salary as claimed is considered excessive for the services rendered.
- (5) The exercising of a discretion must not be influenced by extra-

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neous and irrelevant facts. For instance, salaries should not be disallowed on the grounds that the recipient is also receiving rent from the employer company. Such a fact would be irrelevant to the question of salary.

(6) The discretion must be based on principles correct in law. For instance, it cannot be said that a corporation and the person controlling such corporation are the same—they are separate legal entities. That is all the Pioneer Laundry case decided. The case otherwise was referred back to the commissioner.

If the above rules are followed the exercise of the discretion cannot be challenged in the courts because the court cannot substitute its own opinion for that of the person in whom the power was vested by the statute.

However, it must be established that such person actually exercised the discretion, that he had all the facts available before him and that a decision was reached after due consideration.

The minister has vested in the Commissioner of Income Tax the powers conferred on him by the act and therefore he is the person who must ultimately exercise discretionary powers so conferred and there should be evidence on the files that prior to the notice of assessment being sent the discretion in question was actually exercised by him after consideration of all the relevant facts. It is the duty of the inspectors and the assessors to see that he has before him all such relevant facts.

The high rates of tax make it all the more important that every taxpayer should be treated fairly and not arbitrarily and to insure this treatment with greater certainty and to insure the court's approval, it is proposed to proceed as follows:

PROCEDURE

When the assessor in the district office considers that a ministerial discretion should be exercised which will vary the income as reported by the taxpayer, the following procedure should be followed:

(1) Notice to the taxpayers—This is important

The inspector should write to the taxpayer telling him that the discretionary powers of the act are about to be exercised on whatever is the particular problem, stating it, and invite the taxpayer to submit whatever evidence he thinks appropriate to be considered in exercising of the discretion. If the taxpayer or his representative comes in person to discuss the matter a careful memorandum should be made of the conversation and if deemed advisable, a request made that the taxpayer also set forth his arguments in writing (if not already on file). The taxpayer should submit his memorandum or letter in duplicate.

(2) Notice to head office—

A separate memorandum must be attached to the T.20—
—the T.20 is just an internal document, like a letter, which passes between us—

—identified "Re Discretion", setting forth all of the facts and attaching a copy of the taxpayer's submissions and also containing recommendations from the district office. This memorandum should be signed by the assessor and the chief assessor and/or the inspector.

If the matter has come before the Independent Audit Review Board it should also be signed by them. That is an internal board that is revolving. There are three senior auditors on it and all returns have to come before this

board. If any one of such persons is fundamentally opposed (i.e. not in quantum but in principle) to the others, he should submit a separate memorandum setting forth his views.

(3) Form T-20—Discretion

The factual discretion as a determination will be set forth bluntly on "form T-20 discretion" in duplicate, (a sample is attached hereto) and forwarded with the T-20 "discretionary" memorandum for the signature of the commissioner. It is to be particularly noted that this Form T-20 is not to give any reasons for the disallowance or to refer to any memorandum to inspectors or other memoranda but as stated is to set forth the determination bluntly as closely as possible following the sample referred to. These T-20 discretions will come forward in duplicate, one original to be detached and filed, alphabetically, at head office, in a separate carton for future reference in case of appeal or court action.

I pause to say that the form T-20 on which the determination is set forth bluntly has on the back of it the reasons why discretion has been exercised in this way, but when we go to court we do not give those reasons that are stated on the internal memorandum; we just take that part off and say: There is the discretion, there is the answer and there is the signature. That is all that the court gets because the court has no right to those documents back of the exercise of discretion.

(4) Head Office Procedure

The head office assessor will then either sign the recommendation of the district office or endorse a memorandum thereon, or attach a separate memorandum. The "T-20 discretion" in duplicate will then be submitted to the commissioner with the duplicate district office memorandum. If further particulars are required by head office before submission to the commissioner for signature, such will be requested from the district office as usual by either a T-16 or by letter. If a legal opinion is required this will be submitted by one or more members of the legal staff.

(5) Original "form T-20 discretion" to be signed

The commissioner in the name of the Minister of National Revenue and under statutory delegated authority will then sign one of the original "forms T-20 discretion" which will be on file in head office, as stated.

If the question of exercising the discretion initially arises in head office the T-16 will be returned to the district office requesting them to write the taxpayer and proceed as outlined above.

The T-16 is just a list of the forms that come in.

The idea is that there should, indeed must, be on file evidence that there was a pause before exercising the discretion, that the pause was to give the taxpayer notice of the pending exercising of the discretion, that the taxpayer had an opportunity to submit his considerations, facts and reasons and other material and that in the light of these the minister or the commissioner then made a determination by exercising the power of discretion in relation to the very matter that was the subject under consideration.

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As the members of the district staff are in the best position to judge the facts and circumstances, it is expected that in most cases their report will be the deciding factor. Thus it is important that the report be carefully prepared and be as complete as possible.

The above procedure is only required when it is found that the return as submitted by the taxpayer should be changed and the tax increased by reason of the exercise of the discretionary power.

In other words, it is not required for a 10% depreciation on machinery or something that is well understood and not disputed by anyone.

It is to be observed that disallowances of a minor character in regard to depreciation claimed are quite frequent. In view of this, the procedure hereinbefore referred to of forwarding form T-20 discretion may be dispensed with unless the amount involved is fairly substantial. Where, however, (be the amount of the proposed disallowance large or small) you have reason to believe that the disallowance will be objected to, the form T-20 discretion must be completed.

What is a substantial amount or what is a small amount is a matter of judgment but in exercising the judgment, it should be remembered that an item in a particular year might, in itself, be small, but if the determination of the discretionary matter is to be effective from year to year, or an apparent considerable number of years, then that which is small in a particular year becomes substantial by reason of future rights being involved, which future rights may be in amount larger or smaller than the amount in respect of which the discretion in the particular year is to be exercised, or may be the same.

The point is, future rights are involved.

What is a small thing today may be cumulatively large.

If the matter pertains only to one year, then the amount under consideration would necessarily have to be much larger than if future rights were involved, because it is only to be dealt with once.

A lead as to what is a small amount for one year or what, though small for one year, is large because of its continuing future application, or what is a substantial amount, even for one year, cannot be given, because this memorandum deals with the exercise of the discretion in such a possible variety of circumstances, so the amount being large or small will be determined as such by the district office acting as reasonable persons having regard to other like related circumstances, in other or analogous businesses.

In any case where discretion arises and the taxpayer has consented in writing to the proposed disallowance, the inspector will report accordingly on T-20 and in that case the T-20 discretion form will be dispensed with.

For your information and guidance in principle there is attached a general memorandum on the subject of "discretion".

Now I should like to read this, because it shows our attitude on discretion.

The various members of your staff, and particularly the assessing staff which have to assist in the exercise of a discretion, should take note of the following extracts from a long standing decision in the English courts—

The Court of Appeal held, by a majority, that it was contrary to natural justice for the minister to dismiss the appeal . . . without

giving him (the appellant) a chance of being heard; . . . But the House of Lords held that he had no right to object to the minister's order on these grounds.

Lord Haldane stated—

Those whose duty it is to decide must act judicially. They must deal with the question referred to them without bias and they must give to each of the parties the opportunity of adequately presenting the case made. The decision must be come to in the spirit and with the sense of responsibility of a tribunal whose duty it is to mete out justice but the procedure of each tribunal need not follow the same lines.

Finally Lord Haldane expressed the view that the board was not bound to hear the appellant orally provided he had the opportunity (which was in fact provided) of stating his case.

Lord Shaw rejected the claim that the appellant was entitled to an audience of the particular judge or judges of his appeal, when these had been identified, in order that he might have a personal hearing which should survey the whole of the material available, and disclose the report made on the public local inquiry and the views put forward thereon, by the inspector who conducted it, for the guidance or consideration of the department.

In other words, these documents are confidential.

"If such a disclosure were compulsory" said Lord Shaw, "it would place a serious impediment upon that frankness which ought to obtain among a staff accustomed to elaborately detailed and often most delicate and difficult tasks. The same argument would lead to a disclosure of the whole file containing the views of the entire hierarchy of inspectors, secretaries, assistants, consultants and other officials who had considered the matter, many of whose opinions may differ but all of which form the material for the ultimate decision."

To reveal the process by which this corporate opinion was gradually evolved in the department would, he thought, be not only inconsistent with efficiency and existing practice, but also with the theory of parliamentary responsibility for departmental action.

It was made clear that a government department entrusted by an act of parliament with the exercise of judicial functions need not follow the methods adopted by courts but may employ any rules that appear fair and reasonable for the transaction of business.

Thus an administrative tribunal need not furnish an appellant with the reasons for its decisions, but may merely announce the conclusion, whereas it is the strictly followed custom, in the superior courts of justice, at any rate, to explain at length the reasons which have led the judge to form his decision. Nor need particulars be furnished of the evidence on which the conclusions of the department are based.

Again, the decision of a government department exercising judicial functions need not be conclusive, as in the case of a court. The enquiry may be reopened at any time by the department and the decision revised.

Also, the rule that a fair opportunity be given to each party to present his case is one which will invariably be applied to every tribunal, no matter how wide its powers or how complete its discretion.

No restriction was imposed save that attention should be paid to what has been called "natural justice". It was said in one case that "it is impossible to lay down the requirements of 'natural justice' but the phrase is actually employed to denote two or three elementary principles which, according to English ideas, must be followed by all

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who discharge judicial functions. Thus, it is 'against natural justice' to arrive at a decision before both parties have had an opportunity of stating their case. No one must be condemned unheard."

Questions involving conceptions of economic justice which would not be admissible in the trial of a private claim in an ordinary court of law, have played an important part in determining the questions arising under the Income War Tax Act.

The income tax administration is composed not of judges but of ordinary citizens functioning under a public statute, administering, on the evidence placed before them, economic justice. They are all public officers responsible to the minister in charge of the department, who is responsible to parliament. Each such officer is in a sense an administrative tribunal, in the administration or conduct of public affairs, with power to consider questions primarily of fact within the ambit of the law and the wide powers of discretion given them.

Their decision, upon appropriate approval, becomes binding on private persons, affecting their private rights. Such administrative officers should not make decisions without giving an opportunity to the persons affected of being heard but need not delay if that person does not take advantage of the opportunity to be heard.

Where property rights are involved, as in income tax matters, the courts regard the proceedings of the tribunals, and this would include the district offices, as being in the nature of judicial proceedings, although the forum is a wholly domestic one and in no way bound by so-called judicial procedure. Those acting judicially, however, are required to administer natural justice and natural justice should be dispensed by an unbiased and impartial mind, which officers are required to bring to their tasks.

Such minds should be free from financial interest in the controversy for an officer should not act where he has a personal interest of a financial or property character. Neither should he act in the position, due to bias or prejudice, of accuser and judge.

Therefore, provided the officers administering the income tax act do not infringe the simple provisions relating to natural justice, as referred to, they are free to arrive at whatever decision, having regard to the circumstances and facts, they choose to think proper and to recommend accordingly for its adoption.

Our records should show that an opportunity was given to the taxpayer to consider the proposed changes before they were actually made and if that is done and the simple elements referred to have been adhered to, the exercise of the discretion will not be subject to alteration upon review by any court. They will only alter where natural justice has been infringed. It is right that then they should.

I read that lengthy document because I want you gentlemen to get a complete understanding of our earnest endeavour to instruct many persons, in many parts of Canada, who are assisting in the administration of the law, that they must have a sense of responsibility, a sense of justice, and realize that they are dealing with matters wherein the taxpayer has certain inalienable rights which we must not infringe, and that if the taxpayer thinks we do infringe them he should have an appeal to a court of justice for the determination of his rights. We earnestly endeavour to instruct our officials in these important duties that touch

so deeply the affairs of our people. The procedure is laid down to ensure that the taxpayer gets notice and is given time to think the matter over. The taxpayer is also invited to come into the office and go over the matter in dispute. We try to make it plain to him that he is not dealt with abruptly or arbitrarily.

Now Mr. Chairman and honourable senators, you will note that in the memorandum of instructions I just finished reading we have taken pains to make the rules readily understood and explicit. In doing so we have perhaps made them even more restrictive upon the minister than the courts' judgments would require. We have done so, however, to ensure that the taxpayer got his full measure of justice under the law.

I believe that we have kept our administrative procedure, in practice as well as in theory, strictly within the limits of proper discretionary action as laid down by the courts. The grounds for my belief are twofold:

First, we have filed the inter-office memorandum to which I refer in the Exchequer Court on a number of occasions as part of the evidence submitted on tax cases. No unfavourable comment has been received in respect of it. Nor, I might add, has any favourable comment been received.

Secondly, we have taken six cases to the Exchequer Court and the Supreme Court of Canada in the course of our administration and have so far only lost on one occasion. This was the famous case of *Pioneer Laundry and Dry Cleaners Ltd. v. Minister of National Revenue*, 1940 A.C. p. 127, in which the Privy Council informed us that we had violated a fundamental principle of law by ignoring the rule in the case of *Solomon v. Solomon* that a corporation is a separate entity from its shareholders. That is all that the *Pioneer Laundry* case decided, and the matter was referred back to the minister to exercise his discretion.

This seems to be strong evidence that wherever the discretionary powers have been exercised they have been properly exercised according to the law. This is not to say that they are always desirable or that their exercise is always in the taxpayers' favour but rather that, in so far as parliament has conferred administrative powers upon the minister and those powers have been delegated to me,

I have used them on all occasions in a manner consonant with the rules established by the courts and, as you have noted from the above memorandum, in most cases those rules have been narrowed to restrict me even further.

While on the subject of the memorandum, I should draw your attention to the penultimate paragraph on page 2:

The minister has vested in the Commissioner of Income Tax the powers conferred on him by the act and therefore he is the person who must ultimately exercise discretionary powers so conferred and there should be evidence in the files that prior to the notice of assessment being sent the discretion in question was actually exercised by him after consideration of all the relevant facts. It is the duty of the inspectors and the assessors to see that he has before him all such relevant facts.

In closing I feel that I cannot do better than quote a very telling remark of W. A. Robson found in his book entitled "Justice and Administrative Law" at p. 74:

The executive official, be he inquisitorial, or regulatory, or origina-tive, possesses an inherent right to initiate action by his own motion. Administration without initiation is almost unimaginable in present circumstances. The administrator does not originate continuously; nor does he always originate wisely or effectively. But it is nevertheless an undeniable fact that every administrative body has what an American writer calls "a continuing responsibility for results" of a sort which is unknown to the judge. "It must ferret out violations, initiate proceedings, and adopt whatever proper methods are necessary to enforce compliance with the law." This duty of spontaneous, self-motivated activity may be contrasted with the enforced passivity of the judge, who must wait, spiderlike, till someone enters the web of his jurisdiction.

That concludes my remarks on the delegation of authority and the exercise of discretion. Perhaps I went into these matters in a little too much detail, but I thought it was well to do so because I have heard so much about the hundred discretions. I do not know whether there are one hundred discretions authorized in the act but a good deal of discretionary power is given in connection with one subject and another. The number of times this is mentioned with regard to any particular subject can be counted.

I believe the categories of discretion should be better set forth. The figure of 100 is rather a broad and loose statement. I will now put in a statement on categories of discretion.

1. Allowance of reserves.

- (a) Depletion.
- (b) Depreciation.
- (c) Bad debts.
- (d) Inventory reserves (E.P.T.).

2. Limitation of expenses.
 1. Expenses.
 2. Salaries.
 3. In capital expenditure allowance.
 4. Interest.
 3. Determination of true nature of transactions where lessening of tax may be involved with reference to companies and individuals.
 1. Inter-company purchases and sales.
 2. Value of shareholders' property transferred to company.
 3. Unreasonable payment to non-resident companies.
 4. Transactions between husband and wife and parent and child.
 4. Determination of nature of income.
 1. Interest portion.
 2. Tax free living allowance.
 5. Determining nature and effect of certain legal documents (mortgage and international agreements).
 6. Approval of pension schemes.
 7. Minor administrative discretions.
 1. Extending time for making return.
 2. Require production of letters and documents involved in assessment.
 3. Require keeping of books.
 4. Demand payment of taxes for a person suspected of leaving Canada.
 8. Regulations to carry act into effect.
 9. Waiving penalties.
 1. Failure to file return.
 10. Determination of standard profits.
 - (a) Commencement of business.
 - (b) Nature of business.
 11. Adjust standard profits.
 1. Basis of partial fiscal period.
 2. Alteration of capital.
 12. Direct a reference to Board of Referees in case of new or substantially different business.
- HON. MR. VIEN: Are they all provided for in the act?
- MR. ELLIOTT: They are all provided for in the act.
- HON. MR. VIEN: Could you file a memorandum indicating the references to the sections of the act.
- MR. ELLIOTT: With a good deal of reticence I say yes.

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MR. ELLIOTT: Now, Mr. Chairman and honourable senators, I think I said on the adjournment at the last meeting that I would take up the legal division. I am not going to make a very elaborate statement on the legal division. I am going to state very shortly and in a statistical manner just what its work is, and the position in which it is.

The legal branch is more than its name implies. It is also an administrative division. It has a staff of 40, 13 of whom are professionally qualified lawyers. It deals with all the correspondence that comes to head office that requires the determination of a legal question. I may say the number of letters and documents received and answered will be approximately 12,000 for the current fiscal year. It also answers all the questions that are raised by the audit staff in the examination of taxpayers' affairs, whether the question is raised in the field and sent to head office or raised by head office assessors themselves. These are dealt with by submitting a memorandum to the legal division for decision. It also handles all legal process for false returns, failure to file returns, and failure to pay tax.

People generally believe that the legal branch deals only with appeals but, as indicated, this is wrong, as one of its regular duties is to keep the department in every direction on a well-founded legal base. Needless to say, interviews are a major part of the activities of this branch, as many of the legal members of this committee are aware. The handling of appeals shows that we are approximately on a current basis, so far as anything legal can be on a current basis, because once the matter gets into the channel of legal action, members of this committee are aware of the legal delays. Appeals are of two kinds. The vast majority are simply lodged for the purpose of protecting the taxpayer's right against a possible statute bar or as a basis for discussion of a difference of view, very often relating simply to the facts, but whether of facts or law, appeals are filed as a means of getting some reasonable delay wherein the taxpayer may, by himself or his representative, discuss the matter at an appropriate time with the department. Some, however, are genuine appeals based on different viewpoints of the law.

In the fiscal periods ending March, 1944, 1945, and up

to 10th November, 1945, i.e., in the 1946 fiscal period, or in 31 months we received 2,160 appeals. During the same period we disposed of 2,098 appeals. This represents a rate of disposal amounting to 97 per cent but the 3 per cent lag is misleading inasmuch as in the last year and a half the rate of disposal of appeals has greatly exceeded the inflow. However, what I do wish to leave with the committee is that in the main the flow of appeals is dealt with in an increasingly expeditious manner, and I think this will be found to be so on a further examination by the committee.

As a trend of the times, I might say that in the present fiscal period we are disposing of appeals at a rate much in excess of that at which they are received. For example, for the seven months of the present fiscal period we have received 540 appeals and have disposed of 723. In more detail I gave the committee the following table:

	1943-44	1944-45	1945-46 to 10/11/45	Total
On hand 31st March, 1943 ...				608
Received	912	708	540	2,160
				2,768
Disposed of	505	870	723	2,098
On hand 10th November, 1945				670

Over and above these appeals we have received 158 appeals under the Excess Profits Tax Act, which are clearly protective appeals and will disappear when the standard profits of the appellants are determined. We do not count them as real appeals.

In the administration of any business, be it individual, corporate or government, honourable senators realize that there is nothing more important than the certainty that all things done are within the requirements of the law and that even performing duties within the ambit of the law, particularly in cases of governments, it must be done in a manner that will convey to the party on whom the duty is imposed that it is the law that speaks and not the administration, which is only the instrument of the law. The governments in themselves are so powerful that there is often a feeling among people that by sheer force of that overall concept of power, something is done which, were it not a government, could not be done.

In other words, corporations and individuals would not

act in such a manner. Now, this is a belief that should be dispelled. Though governments are regarded as powerful, nevertheless they factually have no more power than is given by the laws enacted in accordance with well-established constitutional principles. I should like it to be known that the taxation division is always ready in cases of doubt to give that interpretation which will resolve doubtful matters in favour of the party who otherwise would be required to bear the burden. On the other hand, it is equally true that if the person bearing the burden is clearly within the ambit of the law, then the burden must be borne and it is not within the power of the administration to extend relief. Then again, if the person is free or beyond the letter of the law, no matter how much, from an equitable point of view, he should be brought within the ambit of the law, the administration has no power on that equitable belief, to bring the person within the law. In short, he is free.

Contracts between individuals can be adjusted by the individuals, but the statute applies not to one individual but to multiple persons, even in the millions, and a decision therefore must be made in regard to any point raised by a single taxpayer having in mind that whatever that decision is, it must apply with equal force or belief in respect of all other taxpayers who are not present at the particular argument on a particular issue.

In other words, every decision is substantially a multiple decision. The incidents of the law as they evolve through interpretation of the sections of the law must find their impact in an equal manner on every person within the jurisdiction. This concept is not realized by any taxpayers who bring their particular affairs to the division and, having regard to related or extraneous circumstances, not germane to the taxing law itself, request that something be done for them administratively. It should be realized that this is quite impossible. One must be in a position at all times to look any taxpayer in the eye, no matter how onerous the extraneous facts may be, and say with great certainty that that which is being done to him according to the law is equally being done to all other persons within the ambit of the law.

The reputation of the department is sometimes jeopardized in the sense of being harsh by persons who, seeking

clemency, by reason of extraneous facts, cannot find it, and believing in principles of equity, feel aggrieved that their concept of equity was not granted.

It would be desirable if all persons could fully appreciate this fact, and no matter how sympathetic one may be towards this or that general situation, nevertheless administrators are bound by the law in exactly the same manner as the taxpayer is bound by the law. A departure from this concept is the first step towards shaking the whole administration because it is impossible to grant to one and not grant the same privileges to all.

Finally, it should be said that at all times, in every branch of the administration, we not only seek to give that service which has become traditional throughout the Civil Service of Canada, but in all our interpretations and actions we seek to give that fair, large and liberal interpretation which will best attain the true intent, purposes and meaning of the law.

My honourable friends will recognize that last short statement as coming out of the Statute of Interpretation, chapter 1 of the Revised Statutes of Canada.

Now, Mr. Chairman and honourable senators, that is the comment on our legal division statistically, and just to touch on how the legal division must interpret the law and bring all taxpayers who are within it uniformly and equally to equivalent treatment one with the other. . . .

Now, if I may I should like to deal equally as shortly, or even more so, with succession duties. I quite realize, Mr. Chairman, that this is not within the ambit of your order of reference, but it is within the administrative activity, and I think it is work that should be met.

The Dominion Succession Duty Act received royal assent on the 14th June, 1941, and became operative as of that date. Succession duties are mentioned only to show the position of the work in the taxation division. I shall give you a few statistics and record them by handing in a statement, showing returns received—assessable and non-assessable; returns assessed, collections, etc., and giving you the average of our yearly work by the number of returns received and the number dealt with. The work is very substantially current, in fact remarkably so. That is, we are about one month behind, but this lag is rapidly being over-

DISCRETIONARY TAX POWERS

EXHIBIT NO. 8 SUCCESSION DUTY STATISTICS

MARCH 1946.

Year	Number of Dutiable Returns Received	Number of Non-dutiable Returns Received	Total Number of Returns Received	Number of Dutiable Returns Assessed	Number of Non-dutiable Returns Assessed	Total Number of Returns Assessed	Number of Returns on hand at year end	Collections
June 14-Dec. 31								
1941	5,496	16,523	22,019	3,655	10,994	14,659	No record	\$ 4,954,574.19
1942	11,199	31,161	42,360	11,208	31,955	43,163	6,881	13,273,481.43
1943	10,639	30,034	40,673	10,053	29,606	39,559	7,687	15,019,880.85
1944	11,081	31,764	42,845	11,941	33,916	45,857	5,159	17,250,797.83
Jan. 1-Sept. 30							As at Sept. 30	As at Nov. 10
1945	10,214	25,549	35,763	9,365	26,239	35,598	4,699	12,738,541.53
Total	48,529	135,031	183,560	46,227	132,634	178,861		\$66,239,227.83

Number of returns on hand as at Sept. 30, 1945
 Average number of returns received per month
 Number of returns considered as a reasonable number to be on hand
 Average number of dutiable returns received per annum
 Average number of non-dutiable returns received per annum
 Average number of all returns received per annum
 Number of all returns received per annum
 Number of returns presently on hand equivalent to number received in 6 weeks
 Number of returns in Head Office is equivalent to 4 days' work

This has been the average for the past 6 months.

Total number of Succession Duty Staff	260
Total number of different forms in use	34
Number in use by the public	23
Number in use internally	31

Cost of collection is slightly over 3%

taken. 2,500 returns are regarded as being our current work. We always have that many on hand. As everybody knows, succession duty is a tax on the estates of all persons who die domiciled in Canada and on non-resident decedents having assets in Canada. The international double taxation feature, so far as the United States is concerned, has been substantially eliminated by reason of the convention of 1944. No doubt conventions will be entered into with other countries, and there are feelers to that end. It is a very desirable feature when the laws have such onerous rates in them. If I may, Mr. Chairman and honourable senators, I should like to hand in this statement of succession duty statistics in order that you may have a general view. Taking the activities over the period June 14, 1941, when it started up to September 30, 1945, within that span the number of dutiable returns received was, if I may give you round figures, 48,529; the number of non-dutiable returns received was 135,000, making a total of the number of returns received of 183,000. The number of dutiable returns assessed was 46,000 out of 48,000, and the number of non-dutiable returns assessed was 132,000 out of 135,000. The total number of returns assessed was 178,000 out of a total of 183,000.

EXHIBIT No. 8—Statement of succession duty statistics.

Now, the collections during that period amounted to \$66,240,000. It runs about an average of \$15,000,000 per year.

Now, gentlemen, I shall not read any more of the statistics upon this sheet before me, but I think you might be interested when you study the exhibit itself, which is contained in the record.

Succession duties, you all must realize, is not exclusively in the hands of the Dominion.

Going back to my opening introduction, when I asked the question: What is this organization? And in endeavouring to bring to your notice what this organization is, I have made some general notes on the organization itself. Next I dealt with the simplification of laws and forms, and indicated that you might find some difficulty, even as we have. I pointed out the staff situation, and the shortages that we suffer. Then I pointed out the space situation, and the shortages we suffer. I dwelt upon tax deduction at

the source at some length, because it is a brand new feature in our law, and impinges in a marked way upon people who work for wages and salaries. Then I dealt with assessing, and gave you a statistical report on that as well as some comments on the meaning of the word "assessment," and how the law relating to excess profits tax was two years late in its major feature in getting started. Then I dealt with the refunds we have to make, and I observed that they are mentioned in tonight's newspaper. The next thing I dealt with was the refundable portion of the excess profits tax and other taxes, and mentioned that they are about \$444,000,000. Now I have touched a little upon the legal side of our administration and have indicated that we also have succession duties.

In closing I would like to distribute among you charts showing the organization that takes care of all this work, and I shall make a comment or two upon the charts when they are before you in order to enable you to follow the chain of activities. The first chart I suggest that we should examine is the organization chart for head office. You will observe that the deputy minister is at the head, and on the left wing are four boards substantially independent: the Board of Referees under the Excess Profits Tax; the War Contracts Depreciation Board; Wartime Salaries Advisory Committee—I should indicate that I am the Salaries Controller for Canada—and, lastly, Business Classification Committee, Excess Profits Tax Act. I do not think this committee is familiar with the last board. I think you know the others. The Business Classification Committee has arisen by reason of the recent amendment to the excess profits tax law whereby if a business substantially changes the character of its activity it does not have to continue with the standard profits it had given to it or in its own right had under the business as carried on for, say, 1940, 1941, 1942, 1943. The business changes, and they go into a brand new business. For instance, a diamond merchant imported diamonds into Canada, and was a diamond vendor. The war came on, and in due course he decided to be a cutter of diamonds, and set up an organization and personnel and proceeded to cut diamonds. Then he said: "The standard profits which I had as a vendor of diamonds would not do me as the standard profit as a cutter of diamonds. They are two businesses: one is selling merchan-

dise, and the other is manufacturing merchandise." So he puts in a brief that they are engaged in a different business, and that brief is sent to the Business Classification Committee, which is made up of about seven persons: one from our division, two from M. & S., two from Mines and Resources, one from Trade and Commerce, one from National Research. It is a diversified board with no business connections whatsoever; it is composed wholly of senior government servants who have no incentive to put this person or that person out of business, or to be hard on this one or that one. They hear evidence and make a report to the deputy minister, stating whether or not there was a factual change in the business that should be recognized. The cases under that board are growing. That amendment was made only a year ago, and naturally, as people shift into new businesses with the same old corporate structure they come to us to get a standard profit as a new business. This is one of the discretions of the minister. If the minister finds that a new business is carried on, then he may refer the business to the Board of Referees. If he finds it is the same old business with just a change in technique, he does not refer the business to the board. So much for the special boards.

Then we come down to the assistant deputy minister (administration), which speaks for itself, and the assistant deputy minister (legal) and the assistant deputy minister (assessing). Then we have the director of succession duties, and on the extreme right we have the general executive officer, who has a very responsible position. All the mail comes in to him. He distributes it to the appropriate places, so that it may receive early attention by those skilled in that particular subject. What is more important, however, is that when the answers come back in the main they go to this executive officer and he signs the outgoing mail in my name. Naturally he has to watch closely that the rulings contained in these letters are not a departure from well-established rulings of the division because, if one letter gets out that contains a wrong ruling in it, it soon spreads. It goes to the business, and the business speaks to the accountant, and the accountants tell the accounting world, and soon that letter come back many times over! So it is very important that the mail going out is scrutinized in order to see that it contains only the rulings that are cor-

rect. Adverting to the assistant deputy minister (administration) you can see the various sub-headings thereunder. It is a study. If, when looking it over, you desire to ask any questions I shall be glad to answer them.

Similarly, in the case of the legal subdivision, you can see the manner in which it is subdivided, and also in the case of the assessing division.

Now, you observe that there is a linking up and down at the bottom in the "preparation of internal and public forms." That becomes a consultative job between administration and assessors, and naturally the legal division is also concerned. There is, however, directly under "legal" one line I must explain: You will observe that that line is cut off and has nothing at the top. In other words, there has to be a distinct co-ordination of the legal and assessing rulings. They are so interwoven that they must be in constant touch one with the other. In our legal division all these letters that make rulings are indexed both as to the taxpayer and more particularly as to the subject-matter, so that when one goes to the card index of subject-matters and a new letter comes in one will find the latest answer on that question in that drawer, and in that way we have a reference back.

The next chart is headed "taxation division—head office" and this is prepared especially for this committee and for no other purpose, but it is tied up with the chart that you have just examined. For instance, if you look at the first chart on the left you will see "chief accountant" and on the second chart under "assistant deputy minister (administration)" the chief accountant's duties are enumerated: "Receiving remittances from district offices and remitting to Receiver General. Maintaining control accounts with district offices of cash received and taxes levied." Of course, that is a very important matter in order to make sure that the head office is continuously in balance with district offices across Canada. In the district offices there is a daily balance, and between head office and the district offices a quarterly balance, and we have no trouble whatsoever in keeping our proper balances. When I say we have no trouble, like all accounts they have this and that getting out of balance, but we have always come into balance; we have never had to make a special entry, or a journal entry as accountants like to call them, and doctor up something.

That again is a study for you, and you can take it to your rooms.

The third chart refers to a department outside of ours. It is headed "organization chart of a typical district office." It does not fit every office. In the administration of well-founded, like-minded and capable men, of which there are nineteen across Canada, my thought is that you give them the basic outline of what they should do but you do not cut off their own individualities and their own short-cuts and methods of doing a thing that they find expedient, perhaps because of the lay-out of their office. So this is a typical chart. When you visit our offices, as I hope you will, you will find they are not all like this, and could not be. The Toronto district office is laid out on two floors, the whole length of a block running from Yonge street west to Bay street, which is a very long block, and there is a long corridor on the first floor and another long corridor on the next floor up. Those are special circumstances. If the office is on the square plan, you can really lay out the floor space efficiently and follow the flow of the work. This is a typical office and does not fit exactly every office.

The last chart before you is a map of the Dominion of Canada showing the various district offices that we have throughout Canada. The numbers, of course, relate to the legend at the foot on the left side. The irregularity with which our districts were laid out many years ago is explained by the fact that they followed substantially the railways so that mails could move into the central offices with a minimum of exchange of mail from one line to another line and thus avoiding that delay. As many of the honourable senators may know, there was tabled in the House of Commons a few nights ago a proposal to subdivide these nineteen districts into thirty-two districts. That proposal was made after a very careful examination by three gentlemen, two of whom were outside of the government altogether. I think I would like to comment on that for a minute in order to establish confidence in that report on the part of the honourable senators and any other persons who are interested. In the course of the war, when there was a great upswing of numbers and of money of taxpayers received, it was common sense that something should be done to bring the district offices closer to the people. Money was being deducted at the source, and many

of them sent in cash, and we had more cash in our office than we ever had before. We did not like it, but there it was. It amounted to many thousands of dollars, gentlemen. In my judgment the people must be served with a little closer contact by the district offices. So in order to bring about in the most reasonable manner possible, after fully setting out the need for it, I suggested that we should not call in the C. M. A. or the chamber of commerce or labour organizations or farmers' organizations, or any such organizations, nor should we call in businesses that might have an interest, nor call in people in public life to their embarrassment, because you and I know that if they were members of parliament they would have to satisfy their constituencies and might be influenced thereby, might be moved by something other than sheer efficiency in the matter of the location of the district office. So it was decided to ask the Sun Life, to give us a man. They gave us their overall planner, a Scotsman, whose services were free of cost. The next thing was to discover another man who was not very close either to taxes or to these special interests, so we thought the Bell Telephone was close to the public, and we asked the Bell Telephone if they would supply a man for this purpose. They gave us one of their vice-presidents, a Scotsman—I do not know why I say "a Scotsman," because that may be for me or against me!

Then Mr. Wood made the third member of that board of three. These gentlemen from the Bell Telephone and Sun Life had their expenses paid and nothing else. They worked for many months, going to all parts of Canada, and in my judgment they have made a splendid report which I considered very favourable and with which I am heartily in accord. Several months were required to prepare the report, and I commend that report to the government and to everybody who reads it. It cannot be put into effect all at once. It is too big a shift in administration suddenly to supply a district office and take the personnel and ship them to some other place. It has to be done in an orderly well-timed manner. Therefore, gentlemen, do not think that tomorrow there will be thirty-two districts established, because there will not; it will be some long time before they are established. A gentleman spoke to me about closing certain sub-offices, but they will not be closed tomorrow

and may not be closed at all but it is a recommendation by people who have no other interest whatever but to serve Canada to the best of their abilities in the location of these offices, entirely free from any special influence. These gentlemen had no axe to grind; they desired only to give us the best report possible for the kind of work we do.

That is the close of my remarks, Mr. Chairman, and again I would like to say, as I have said in the beginning, that the income tax division welcomes the inquiry. May I repeat our offer to give you every assistance. We are all Canadian citizens, each serving the country in accordance with the place we occupy and likewise in accordance with our abilities. We serve with one end in view, namely, the welfare of Canada and her people. However, the privileges and rights we have must be paid for according to his or her ability to pay, and the administration of the law; also the subdivisions of the work and the officers in charge of them. That work will always be thought of and carried out with the highest motives possible. I thank you, Mr. Chairman, and thank you, honourable senators.

Current Accounting Literature

By Frank S. Capon, C.A.

Montreal, P.Q.

THE University of Kentucky has published a comprehensive and interesting pamphlet on the Kentucky State Budget System (Bulletin No. 11 of the Bureau of Business Research, School of Commerce). The history of financial control and budgeting in Kentucky is traced, and the present system is discussed in detail, covering the general policy planning of such activities as welfare, education, conservation and so forth, the ascertainment of expected cost of the programs, submission of plans and reports to the legislature, authorization by the legislature, and finally the carrying out of the plan as approved. While there are inherent weaknesses in the Kentucky system, these are admitted and explained, so that the entire pamphlet is valuable as a complete treatise on a government budget system from both the executive and legislative viewpoints.

Accounting for Fully Depreciated Assets

Special depreciation and amortization during wartime has resulted in many cases in new units being written off either completely or substantially during short periods, and often it is now found that these assets will be of greater post-war value than was originally estimated. The special bulletin No. 6 in the research series of N.A.C.A. bulletins, dated 1st January, lists the problems that can arise under these circumstances, and discusses the pros and cons of the various accounting treatments. While no hard and fast rules are laid down, the bulletin provides an accounting treatment to meet almost every type of case.

Salvage Can Be Important

An unusual and very interesting article on the operation of a salvage division in a large manufacturing concern is presented by F. E. Lockrow in the 1st January N.A.C.A. Bulletin. In this case, a special organization has been set up to handle salvage throughout the plants, to concentrate on making money out of waste that might well be discarded by supervisors concerned primarily with obtaining production of finished goods. Since annual revenue of over \$1,000,000 is earned by this organization, which is concerned with salvage alone, it can be seen that there is a profitable field here for almost any company.

Incentive Wage Plan

In the same bulletin, C. M. Reinherr and P. Griek explain the details of an incentive wage plan, and the procedure necessary for its installation, operation, and acceptance

PUBLICATION ADDRESSES, AND PRICE PER COPY POSTPAID

- Accountancy, Incorporated Accountants' Hall, Victoria Embankment, London, W.C. 2, England. 1 shilling.
 Accountants' Magazine, 23 Rutland Square, Edinburgh, Scotland. 1s. 3d.
 Accounting Review, School of Commerce, Northwestern University, Evanston, Ill., U.S.A. \$1.
 The Accountant, Moorgate Place, London E.C. 2, England. 1 shilling.
 The Controller, 1 East 42nd St., New York, N.Y. 50 cents.
 Cost and Management, 66 King St. East, Hamilton, Ont. 35 cents.
 Harvard Business Review, Harvard University, Boston, Mass., U.S.A. \$1.50.
 Journal of Accountancy, 13 East 41st St., New York, N.Y. 35 cents.
 The Internal Auditor, 39 Atlantic Street, Stamford, Conn., U.S.A. \$1.
 National Association of Cost Accountants, 385 Madison Ave., New York. 75 cents.
 Taxes—The Tax Magazine. CCH Canadian Limited, 31 Willcocks St., Toronto, Ont. 35 cents.

by employees. Also included are specimens of the schedules necessary to compute incentive wages and prepare reports for management.

Cost Accounting for Home Building

Those interested in costing in the house building industry should review the third article in the above bulletin, which provides a detailed card of accounts and other data for a home building cost system.

Payroll System

In the 15th January N.A.C.A. Bulletin, F. L. Haskell has submitted in detail a case study of a payroll system, from the labour tickets, through the summarization and allocation of labour costs, to the preparation of the employees' earnings record. Many interesting points are brought out, including some novel methods of saving clerical work.

Planning of Employee Benefit Plans

During the war years there has been a phenomenal growth in employee pension and benefit plans, at a time when it appeared that much employee goodwill could be obtained at a nominal net cost after taxes. In the post-war years, the emphasis will be on lower costs, and decreased profit margins, probably rendering difficult the maintenance of expensive employee pension and other plans. The importance of planning in this regard cannot be over-emphasized, and all accountants will be interested in the article on the subject by G. Simons in the 15th January N.A.C.A. Bulletin.

Cartels

Those who are interested in a reasonable and equitable solution of the problem of control of international and national cartels will find much food for thought in the editorial in the 5th January issue of "The Accountant". The entire problem has been so confused with political prejudices and ideologies that we sometimes forget many of the actual facts.

Profits and Stock Valuation

Under the above title, K. Lacey has contributed in the 15th December issue of "The Accountant" what is, without doubt, one of the outstanding articles on inventory valuation for many months. He tears to shreds the case for first-in, first-out valuation, and also the closely related average cost method; and, not being content to condemn them

on accounting grounds alone, goes on to show how these accepted valuation methods are actually a major factor in starting or accentuating business booms and depressions. To many, Mr. Lacey's case will seem irrefutable against the inventory valuation bases at present accepted without question by accountants in most countries, even though he agrees that, for purely theoretical balance sheet purposes, the accepted bases have merit. However, because they ignore basic business facts and are actively harmful to the interests of the community, he calls on accountants to do some thinking, and to resist the temptation to throw the problem to the economists. No accountant should miss this article.

Lifo and Fifo

The 15th December issue of "The Accountant" contains an outstanding editorial concerning inventory valuation, having particular regard to LIFO and FIFO. The editor appeals to accountants to ignore the red herring of taxation that has been dragged across the arguments on inventory valuation, and to study the possible economic effects of accounting decisions on stock valuation. The problem is stated with admirable clarity, and the possible repercussions of ill-thought-out decisions are emphasized.

Form of Annual Reports

Much has been said recently on the subject of corporation annual reports—what they should or should not contain, to whom they should be directed, how they should be set up and printed, and so forth—but seldom have there been articles so sound, so well-reasoned, and so restrained as that by Dr. Lewis H. Haney in the January issue of "The Controller". Dr. Haney gives us a timely reminder that annual reports are still intended for shareholders, even though government, labour, consumers, competitors, and others are also interested, often antagonistically; and he denounces scathingly the flamboyancy of many reports, the excessive use of art work, coloured charts, advertising material, and so forth. Shareholders are interested in economy and efficiency, and will be impressed by a dignified, plain report which gives the impression of a sound investment, carefully managed. After setting forth in some detail the data that should be included, Dr. Haney impresses on the reader that the annual report is a job for the controller or

treasurer, not the public relations expert or the advertising manager.

Review of Reviews

Thomas H. Sanders has made a "Review of Reviews of Accounting Progress" in the January "Journal of Accountancy". This is, in fact, a review of the tenth annual report of the S.E.C. in the United States and the report of the Cohen Committee in the United Kingdom. These two reports actually review accounting progress in the two countries in the past decade, and Mr. Sanders' summary is a valuable periodic stocktaking.

Appraisal of Fixed Assets

The relationship of the accountant and the appraiser is the subject of an article by C. Crocheron in the January "Journal of Accountancy". Apart from outlining the interdependence of the two professions in the realms of fixed asset and depreciation accounting, Mr. Crocheron discusses briefly appraisal principles and procedures.

Trends in Accounting

The remarks on accounting trends by William Werntz in the January "Journal of Accountancy" are authoritative, since he is chief accountant for the Securities and Exchange Commission. After stressing the growing importance of the income statement, he illustrates the effect that varying accounting principles can have on reported income by citing cases where per share earnings could vary from 36 cents to \$1.79 or from \$3.01 to \$1.60 merely by adopting different but generally accepted accounting techniques. Finally, Mr. Werntz calls for disclosure of greater detail, including a breakdown of both sales and cost of sales according to products or other bases—this may be going a little far in Canada, where companies have yet to be convinced that there is a good case for the disclosure of total sales and cost figures.

Provincial News

Manitoba

The Institute of Chartered Accountants of Manitoba announce that the following are the successful candidates of the Institute in the uniform examinations of December 1945, set throughout the Dominion by a joint committee consisting of representatives of the provincial institutes of chartered accountants.

Final. *Complete pass:* Acton Henry Chalu; Elmer Delford Daum; Marion Cathie MacTaggart; Claude A. Ramp-ton; Kenneth Hugo Smith; Mark Whitley Smith; Alex Tadman.

Pass in Accounting only: Thomas Brown Milne; Charles R. Peirson.

Marion Cathie MacTaggart was awarded the War Memorial Gold Medal and prize of \$100.00 donated by the Institute of Chartered Accountants of Manitoba for ranking highest among the Manitoba candidates.

Intermediate. *Complete pass:* Harry Mitchell Belyea; John Kemp A. Brown; Keith Wilson Campbell; William Albert Code; Margaret Lyall Donald; Abraham Adolph Frankel; Mac Cameron Govier; Doris Karn; James Kenneth G. Laird; Alexander K. McKean; Bruce K. Pell; Isadore Peltz; James Reid; John Allen Roberts; Arthur Stannard; William Bruce Still; Stanley Frederick Tait; Leonard Gilbert Walker.

Isadore Peltz, who secured first place among the Manitoba candidates, was awarded the W. A. Henderson Silver Medal, and a scholarship of the value of \$50.00.

Ontario

The Institute of Chartered Accountants of Ontario announces that the following candidates were successful in the December 1945 examinations:

Primary: J. Adamson; J. R. Backus; Miss M. C. Barnett; L. J. Beeson; L. Bennet-Alder; J. W. Bennett; Miss S. B. Birchard; J. W. Blodgett; A. S. D. Bounsall; D. W. Bourne; H. F. Brockman; J. G. Brown; K. J. Bryant; E. F. M. Cachia; G. Colvin; S. T. Down; C. P. Dykes; K. H. Emerton; M. Feldman; P. E. Fleming; M. Flicht; G. C. Foxall; Miss D. Gamble; C. Hallam; J. R. Hilborn; H. Isenbaum; E. T. Jewitt; K. C. Jolley; K. B. Kirkwood; P. Krauel; Miss B.

Ladd; N. A. Leousis; D. F. Lind; B. N. Lynd; W. D. Mac-Millan; H. A. Manuel; Miss R. Merker; P. Milhalovitz; D. Miller; G. T. Mills; D. K. Morrison; Miss V. Morrow; W. F. McCormick; A. F. K. McGill; J. A. McKee; P. W. Newton; G. T. O'Gorman; J. C. Pattinson; L. A. Pearce; H. G. Robertson; E. Robinson; N. Rubinoff; W. J. Schaefer; S. Shoom; H. F. Singleton; D. F. Starling; C. H. Tod; J. F. Tomsich; J. L. Trudeau; T. Van Zuiden; W. A. Witham; L. W. Zeifman.

Intermediate: Miss H. Archer; J. O. Arnold; E. M. Auger; R. A. Blair; A. Bohnen; W. B. Bolton; L. J. Butler; B. Caplan; V. H. Chadwick; A. T. Coates; H. D. Counter; R. Crolly; J. M. Dooley; J. A. Downey; N. H. Easson; G. H. Ferris; H. Gedansky; A. F. Gregory; H. C. Haney; V. N. Harbinson; M. Harris; N. B. Heffernan; F. F. Howarth; Mrs. E. M. F. Madill; N. B. Mathewson; A. Merkel; E. B. Meyers; H. C. Middleton; J. C. Murdoch; C. S. McLaren; Miss L. McLeod; A. R. McPhie; L. W. Pastorius; G. D. Pattison; Miss A. C. Ratney; R. C. Reed; G. W. Riehl; D. G. Rigby; Miss M. Seaton; J. H. Sheard; Miss E. Sheldon; A. Sorrell; D. H. Stodart; R. B. Vopni; N. M. Watt; J. C. White; J. E. Wolfram; E. D. Wood; R. G. Woods; D. F. Wyckoff; M. A. Young.

Final: H. A. Agar; G. R. Boyer; G. E. Browning; M. Cassels; F. L. DeGuerre; G. B. Donaldson; N. D. H. Evans; J. H. Ewart; C. F. Flaman; J. Gluskin; B. Gordon; H. Hacker; W. F. Harvie; A. J. Horning; J. E. Kearney; F. D. Kemp; W. E. Kennedy; J. Kew; G. Moller; A. P. McDiarmid; L. I. Papoff; J. A. Partridge; M. S. Richman; J. P. Robertson; A. J. Saunders; S. R. Scott; F. L. Taylor; Miss M. J. Trench; J. H. Turner; J. E. Walsh; C. F. Wilson; R. A. Woolsley; J. E. Young.

Granted Supplementals: T. C. Adams, Accounting I and III; P. T. Barnes, Auditing; F. A. Bennett, Economics; K. R. Church, Auditing; M. Cole, Accounting III and IV; J. A. Durfey, Accounting four papers; J. Fink, Economics; N. Freeman, Auditing; D. A. Harwood, Auditing; A. G. Holman, Accounting four papers; R. E. F. Jones, Auditing; M. A. Leroy, Auditing; A. G. Rankin, Accounting four papers; W. G. M. Robinson, Auditing; L. G. Sayers, Auditing; R. S. Slater, Auditing and Economics; W. J. Snowball, Economics.

OBITUARIES

The special prizes provided each year have been awarded to the following candidates in the 1945 examinations:

Primary: Institute first prize, D. K. Morrison; Institute second prize, P. Krauel and T. Van Zuiden.

Intermediate: Institute first prize, A. Merkel; Institute second prize, N. M. Watt.

Final: Institute gold medal, A. J. Saunders; George Edwards prize, G. E. Browning; W. T. Kernahan prize, C. F. Flaman; E. R. C. Clarkson prize, R. A. Woolsley.

The special prize to the ex-serviceman who was successful in the final examination and received the highest marks was awarded to J. E. Walsh.

Personals

Lawrence H. Newnham, C.A., announces the opening of an office for the practice of his profession at 56 Adelaide Street East, Toronto.

McIntosh & Harder, chartered accountants, Vancouver, B.C., announce the admission to partnership of J. Stanley McVicar, C.A., and that henceforth their practice will be conducted under the firm name of McIntosh, Harder & McVicar, chartered accountants, 514 Standard Bank Building, Vancouver.

Obituaries

The Late Harry Holden Bamford

The Institute of Chartered Accountants of Saskatchewan announces with deep regret the sudden death of Harry Holden Bamford, at the age of sixty-five, in Moose Jaw, on January 11.

Born in England, Mr. Bamford came to Canada with his parents in 1884, settling at Bird's Hill, near Winnipeg, and later at Selkirk, Manitoba, and in 1899 came to Moose Jaw. He was admitted to the Institute of Chartered Accountants of Saskatchewan in 1923 and shortly afterwards entered into partnership with the late Mr. W. E. Hodge, practising in Moose Jaw. He was elected a fellow of the Institute in 1935.

A veteran of the first world war, Mr. Bamford served

in Canada and England as paymaster of the 128th Battalion, C.E.F., holding the rank of Captain. In France he served with the 5th C.D.A.C. For his services in World War I he held the general service medal and the Victory medal and later was awarded the Canadian Efficiency Decoration.

Mr. Bamford was a prominent member of the Anglican Church. He was a member of the Council of the Institute of Chartered Accountants of Saskatchewan during 1928-1934, holding the office of vice-president 1930-1932 and president 1932-1934, and was representative of the Institute on the Senate of the University of Saskatchewan. A charter member and past president of the Moose Jaw Kiwanis Club, Mr. Bamford was also a member of the Moose Jaw Masonic Lodge, being a past master and past district deputy grand master, a member of the Canadian Legion, a past president of the Moose Jaw Board of Trade and a former member of the Moose Jaw City Council.

Mr. Bamford is survived by his widow, one son, Ralph L. Bamford, C.A., and a sister, Mrs. H. Davison Pickett, all of Moose Jaw, to whom the Institute offers its sincere sympathy.

The Late Lord Plender

The Institute of Chartered Accountants of Ontario regrets to announce the death of The Right Honourable Sir William Plender, Bt., G.B.E., LL.D., F.C.A., at the age of 84, at Tunbridge Wells, England, on January 19, 1946. Lord Plender was senior partner in the firm of Deloitte, Plender, Griffiths and Co., and was admitted to the Ontario Institute in 1931.

Throughout his career Lord Plender served his country with untiring zeal and his public services were rewarded by a knighthood in 1911, the G.B.E. in 1918, a baronetcy in 1923, and a barony in 1931. He was president of the Institute of Chartered Accountants in England and Wales in 1910-11, 1911-12 and 1929-30, and also of the fourth International Congress on Accounting held in London in 1933. Lord Plender's activities were not confined to the accounting profession, and the many offices and honours which came to him testified to the diversity of his interests and services.

STUDENTS' DEPARTMENT

R. G. H. SMAILS, C.A., Editor

NOTES AND COMMENT

We had always thought it would happen sooner or later. Now, apparently, it has happened for P. M. Richards reviewing in a recent issue of *Saturday Night J. C. McConnell*, *I Speak for the Centre*, seems to have found an author who attributes the major part of the world's economic ills to the bad habits of accountants. "Our accounting practice", says Mr. Richards, in presenting the author's argument, "assumes that the value of capital remains fixed. By common consent we have given to our money the quality of indestructibility. Financial capital is not allowed to depreciate, though we know that physical capital does. Our whole financial practice is based on this illusion Instead of adding depreciation charges to the price of goods and thereby raising prices, curtailing purchasing power and contracting production, the practice should be to write down the capital value to record its depreciation." [sic]. Mr. Richards then goes on to quote directly from the book the author's plan for a "streamlined accounting adapted to the technology of change." By the use of such a system we are told "every year the dead capital values are marshalled off the stage by certified public accountants. New capital values are taking their place. All values are falling uniformly. Purchasing power and living standards are rising in the same proportion. In this way, by conforming to the natural law and the requirements of a monetary measure industry will at last escape the fluctuations of the business cycle and realize the essential conditions for an expanding economy under the rule of social justice."

This is all a little confusing for the accountant but we take Mr. McConnell to be advocating that depreciation of fixed assets should be written off capital instead of being charged as a part of the cost of goods produced. This puts us in mind of Mr. Gilbert Jackson's cynical friend well versed in financial matters, who said it was the function of capital to be lost anyway. That, he claimed, was just what capital was for. It also reminds us that we have on several occasions heard our economist friends inveighing against

depreciation charges as a form of savings which are not always promptly reinvested, and which if not promptly reinvested reduce the purchasing power of the community and the demand for consumer goods.

Well we are quite sure that accountants would be willing to treat depreciation as loss of capital instead of expense if by so doing they could save the economic world. But how would accountants then dispose of their savings (supposing they were in a position to save)? Presumably by contriving not to have any savings.

PUZZLE

An aeroplane carrying as passengers fifteen Arabs and fifteen Jews, developed engine trouble, and the pilot declared that in order to save the ship and crew one half of the passengers must be thrown out. It was agreed that the passengers' names should be arranged in a circle and that every ninth name, reckoning from a certain point should be a victim. What arrangement would save all the Arabs or all the Jews?

SOLUTION TO LAST MONTH'S PUZZLE

The fallacy lies in the fact that each side of the equation equals zero. Zero divided or multiplied by one gives the same quantity as zero divided or multiplied by a million. It is no proof that the divisors or multipliers are equal numbers.

PROBLEMS AND SOLUTIONS

THE PROVINCIAL INSTITUTES OF CHARTERED ACCOUNTANTS

Solutions presented in this section are prepared by practising members of the several provincial Institutes and represent the personal views and opinions of those members. They are designed not as models for submission to the examiner but rather as such discussion and explanation of the problem as will make its study of benefit to the student. Discussion of solutions presented is cordially invited.

PROBLEM I

FINAL EXAMINATION, DECEMBER 1944

Accounting IV, Question 3 (25 marks)

The trial balance of the general ledger of the Saskatoon branch of the Invasion Trust Company showed the following balances as at 31st December 1943:

Capital (or own) account section (or division)	
Office premises	\$ 50,000
Real estate held for sale	2,000
Mortgages, loans receivable	20,000

STUDENTS' DEPARTMENT

Dominion of Canada bonds 3% 1957	5,000	
Transfer fees receivable	1,000	
Loan to trust account	3,000	
Cash in bank	8,000	
Interest receivable on mortgages	250	
Unearned rents—safety deposit vaults		\$ 490
Head office account—1st January 1943		87,350
Commission and agency revenue		55,000
Interest earned on guaranteed funds (net) ..		16,000
Safety deposit vault rental income—less expenses		2,600
Management and office salaries	44,750	
Office and general expenses	25,350	
Depreciation on office premises	2,000	
	<u>\$ 161,350</u>	<u>\$ 161,350</u>

Guaranteed account section (or division)

Guaranteed mortgages, loans receivable ...	\$ 580,000	
Dominion of Canada bonds	70,000	
Guaranteed mortgage, interest receivable ..	1,800	
Guaranteed cash in bank	15,000	
Guaranteed funds		\$ 560,000
Head office—guaranteed account		106,800
	<u>\$ 666,800</u>	<u>\$ 666,800</u>

Trust estates and agencies account section (or division)

Investment mortgages receivable	\$1,830,000	
Call loans on bonds	10,000	
Investment mortgage interest receivable ...	1,700	
Cash in banks	390,000	
Investment liabilities to trust estates		\$1,841,700
Corpus or capital ledger control		220,000
Revenue ledger control		167,000
Advance from capital account		3,000
Original mortgages receivable	600,000	
Original stocks and bonds	2,590,000	
Real estate	1,310,000	
Rents receivable	3,500	
Original mortgage interest receivable	3,250	
Original liabilities to trust estates		4,376,750
Real estate—mortgage liability		130,000
	<u>\$6,738,450</u>	<u>\$6,738,450</u>

Required:

(a) Submit cash and other entries in journal entry form without journal narrative to record the following adjustments, ignoring income taxes:

Commission and agency revenue has been understated by the sum of \$2,000 due to an omission whereby a fee of that amount was not charged to a client's account in the revenue ledger. The sum of \$5,000 is required to provide for a loss in the guaranteed mortgage loans receivable to be charged against the operations of the branch for the year. A loss of \$8,000 on the sale of original stocks and bonds (held for clients) had not been recorded as at 31st December 1943.

THE CANADIAN CHARTERED ACCOUNTANT

(b) Prepare a statement of profit and loss and balance sheet of the capital, guaranteed and trust divisions, to be submitted to head office.

SOLUTION
THE INVASION TRUST COMPANY
SASKATOON BRANCH

(a) **ADJUSTING ENTRIES AS AT 31st DECEMBER 1943**
IN JOURNAL ENTRY FORM (WITHOUT JOURNAL
NARRATIVE)

<i>Capital (or own account) Division:</i>			
Cash in bank	\$2,000		
To Commissions and agency revenue		\$2,000	
<i>Trust Division:</i>			
Revenue ledger control	2,000		
To Cash in bank		2,000	
<i>Capital Division:</i>			
Profit and Loss	5,000		
Provision for loss on guaranteed mortgages	\$5,000.00		
To Cash in bank		5,000	
<i>Guaranteed Division:</i>			
Cash	5,000		
To Reserve for loss on guaranteed mortgages		5,000	
<i>Trust Division:</i>			
Original liabilities to trust estates	8,000		
To Original stocks and bonds		8,000	

(b) **THE INVASION TRUST COMPANY**
SASKATOON BRANCH
CAPITAL DIVISION
STATEMENT OF PROFIT AND LOSS
FOR THE YEAR ENDED 31st DECEMBER 1943

<i>Revenue:</i>			
Commission for management of estates, agencies, etc.		\$57,000	
<i>Guaranteed interest:</i>			
Net profit on guaranteed funds		16,000	
Safety deposit vault rentals less expenses		2,600	
		<u>75,600</u>	
<i>Deduct—</i>			
<i>Expenditures:</i>			
Management and office salaries	\$44,750		
Office and general expenses	25,350		
Depreciation on office premises	2,000		
Provision for loss on guaranteed mortgages ..	5,000		77,100
Loss for the year ended 31st December 1943 carried to Head Office Account (Balance Sheet) ..			<u>\$ 1,500</u>

THE INVASION TRUST COMPANY
SASKATOON BRANCH
BALANCE SHEET AS AT 31st DECEMBER 1943
CAPITAL DIVISION

<i>Assets</i>			
Office premises — at cost		\$ 50,000	
Real estate held for sale		2,000	

STUDENTS' DEPARTMENT

Mortgage loans	\$ 20,000	
Interest receivable on mortgages	250	20,250
		<hr/>
Dominion of Canada bonds 3% 1957—at cost		5,000
Transfer fees receivable		1,000
Loans to trust division		3,000
Cash in chartered bank		5,000
		<hr/>
		\$ 86,250
		<hr/>

Liabilities

Unearned rents		\$ 400
Head Office Account—		
Balance 1st January 1943	\$ 87,350	
Deduct—		
Loss for the year ended 31st December 1943	1,500	
		<hr/>
		85,850
		<hr/>
		\$ 86,250
		<hr/>

GUARANTEED DIVISION

Assets

Mortgage loans	\$580,000	
Deduct—		
Reserve for loss on guaranteed mortgages ..	5,000	
		<hr/>
	\$575,000	
Interest receivable on mortgages	1,800	
		<hr/>
		\$576,800
Dominion of Canada bonds		70,000
Cash in chartered bank		20,000
		<hr/>
		\$666,800
		<hr/>

Liabilities

Funds held under guaranteed investment certificates		\$560,000
Balance due to head office		106,800
		<hr/>
		\$666,800
		<hr/>

TRUST DIVISION

ESTATES, TRUSTS AND AGENCIES:

Investments negotiated by the company
and cash in chartered banks—

Investment mortgages	\$1,830,000	
Interest receivable on mortgages	1,700	
		<hr/>
	\$1,831,700	
Call loans on bonds	10,000	
Cash in chartered banks	388,000	
		<hr/>
		\$2,229,700

ORIGINAL VALUE OF ESTATES AND AGENCIES AT INVENTORY VALUES:

Original mortgages	\$ 600,000	
Original mortgage interest receivable	3,250	
		<hr/>
		\$ 603,250

THE CANADIAN CHARTERED ACCOUNTANT

Original stocks and bonds	2,582,000	
Real estate	1,310,000	
Rents receivable	3,500	
		<u>4,498,750</u>
		<u>\$6,728,450</u>
<i>Liabilities</i>		
<i>ESTATES, TRUSTS AND AGENCIES:</i>		
<i>Trust funds for investment</i>		
<i>or distribution—</i>		
Investment liabilities to trust	\$1,841,700	
<i>Corpus—</i>		
Clients' balances	\$ 220,000	
<i>Add—</i>		
Loan from Capital division ...	3,000	
		<u>223,000</u>
<i>Revenue—</i>		
Clients' balances	165,000	
		<u>\$2,229,700</u>
<i>INVENTORY VALUE OF ORIGINAL ASSETS OF ESTATES</i>		
<i>AND AGENCIES UNDER ADMINISTRATION:</i>		
Original liabilities to trust	\$4,368,750	
Real estate mortgage liabilities ..	130,000	
		<u>4,498,750</u>
		<u>\$6,728,450</u>

PROBLEM II

FINAL EXAMINATION, DECEMBER 1944.

Accounting IV, Question 5 (15 marks)

From the following particulars prepare a statement showing the source of new assets and their application during the year ended 31st December 1943 and a statement of comparative working capital as at 31st December 1943 and 1942.

ALLIED COMPANY LIMITED COMPARATIVE BALANCE SHEETS

	31st December	
	1943	1942
Cash	\$ 300,000	\$ 170,000
Call loan	200,000	.....
Marketable securities	220,000	100,000
Customers' notes and accounts receivable	300,000	250,000
Inventories	160,000	100,000
Investment in affiliated company	180,000	200,000
Deferred charges .....	.....	70,000
Deposit on account of new construction	140,000	.....
Land	50,000	50,000
Plant and equipment	1,950,000	1,350,000
Goodwill .....	.....	200,000
Discount on funded debt	50,000	20,000
	<u>\$3,550,000</u>	<u>\$2,510,000</u>

STUDENTS' DEPARTMENT

<i>Liabilities</i>		
Accounts payable	\$ 200,000	\$ 150,000
Purchase money obligations—current		120,000
Wages payable	40,000	20,000
Reserve for depreciation	600,000	400,000
Mortgage payable		350,000
Funded debt:		
First mortgage six per cent bonds	1,000,000	.....
Premium on sale of common shares	170,000	.....
Share capital—common	1,000,000	800,000
Earned surplus	540,000	670,000
	<u>\$3,550,000</u>	<u>\$2,510,000</u>

<i>Surplus Account</i>	
Balance 1st January 1943	\$670,000
Net profit for the year ended 31st December 1943	200,000
Marketable securities—appreciation	70,000
	<u>\$940,000</u>

Deduct:

Dividends:

Cash	\$ 90,000
Stock	90,000
Goodwill—written off	200,000
Discount on bonds	20,000
	<u>400,000</u>

Balance 31st December 1943	<u>\$540,000</u>
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SOLUTION

ALLIED COMPANY LIMITED

STATEMENT OF SOURCES AND APPLICATION OF NEW ASSETS FOR THE YEAR ENDED 31st DECEMBER 1943

Sources of new assets:

Net profit for the year ended 31st December 1943	\$ 200,000
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Add—

Charges to operations not involving a cash outlay during the year:

Depreciation	\$ 200,000
Decrease in deferred charges	70,000
	<u>270,000</u>
	<u>\$ 470,000</u>

Proceeds of sale of first mortgage six per cent bonds	\$1,000,000
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Less—

Discount on first mortgage bonds	50,000
	<u>950,000</u>

Proceeds of sales of common shares:

Par value of shares sold	\$ 110,000
Premium on shares sold	170,000
	<u>280,000</u>

THE CANADIAN CHARTERED ACCOUNTANT

Sale of investment in subsidiary company ..	20,000
	<u>\$1,720,000</u>
<i>Deduct—</i>	
<i>Application of assets:</i>	
Deposit on new construction	\$ 140,000
Expenditures on plant and equipment ..	600,000
Retirement of first mortgage	350,000
Dividend paid in cash on common shares	90,000
	<u>1,180,000</u>
Excess of new assets provided over assets applied represented by increase in net work- ing capital as per statement attached	<u>\$ 540,000</u>

STATEMENT OF COMPARATIVE WORKING CAPITAL AS AT 31st DECEMBER 1943 AND 1942

	31st December 1943	1942	Working Capital Increase or Decrease
<i>Current assets:</i>			
Cash	\$ 300,000	\$170,000	\$130,000
Call loan	200,000	.....	200,000
Marketable securities	\$220,000		
<i>Less—</i>			
Reversal of appreciation 70,000	150,000	100,000	50,000
Customers' notes and accounts receivable	300,000	250,000	50,000
Inventories	160,000	100,000	60,000
	<u>\$1,110,000</u>	<u>\$620,000</u>	<u>\$490,000</u>
<i>Current liabilities:</i>			
Accounts payable	\$ 200,000	\$150,000	\$ 50,000
Purchase money obligations .....	.....	120,000	120,000
Wages payable	40,000	20,000	20,000
	<u>\$ 240,000</u>	<u>\$290,000</u>	<u>\$ 50,000</u>
Increase in net working capital	<u>\$ 870,000</u>	<u>\$330,000</u>	<u>\$540,000</u>